



FINANCIAL LEVERAGE AND TIMELINESS OF AUDIT REPORTING OF LISTED INDUSTRIAL GOODS FIRMS IN NIGERIA

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Abstract

Exceptionally leveraged firms need extensive auditing time and standard auditing services which are carried out by hiring qualified auditing firms, with such auditors putting in more time to investigate authenticity of the debts with managers of such companies obligated to relate more information in their audited annual reports and accounts which may lead to probable delay in timeliness of audit reporting. The study therefore, examined effect of financial leverage on timeliness of audit reporting of listed industrial goods firms in Nigeria. The population of the study comprised all the 14 listed industrial goods firms on the floor of the Nigerian Stock Exchange (NSE). A purposive sampling technique was used to arrive at a sample size of thirteen (13). The research used secondary sources of data collection covering a period of seven (7) years from 2012 to 2018. The dependent variable is timeliness (TML) while the independent variable is Financial Leverage (LEV) and Size of the company (SZCOM) is the control variable. Multiple regression analysis with Random Effects Model was employed to analyse data. The panel data result which was estimated through the use of Ordinary Least Square (OLS) method showed that LEV is statistically significant; hence, has significant effect on audit report timeliness. The study concludes among others that a decrease in financial leverage result to an increase in timeliness of audit report. It is therefore recommended that, as the amount of leverage used by listed industrial firms in Nigeria should be reduced, the lesser the leverage, the more timely the audit reports.

Keywords: Agency theory, Audit Report, Financial Leverage, Industrial firms, Timeliness.

1. Introduction

Leverage is engaged to avoid using too much equity to fund operations. Excessively amount of financial leverage increases the risk of failure, since it becomes more difficult to repay debt. Highly leveraged firms call for extensive auditing time and require high standard auditing services through the hiring of qualified auditing firms with such auditors putting in more auditing time to investigate authenticity of the debts and managers of such companies are to relate more information in their audited annual reports and accounts which may lead to delay in timely reporting. According to Ibrahim, Nyor and Lateef (2019), the degree to which a company uses fixed-income securities, such as debt and preferred equity, is referred to as financial leverage. Financial leverage can also be seen as the additional volatility of net income caused by the presence of fixed-cost funds. It is the capacity of an organisation to utilised debt in its capital structure. It is also a measure of how much firms use equity and debt to finance their assets.



Audit report is a “written opinion of an auditor regarding an entity's financial statements. It is written in a standard format, as mandated by Generally Accepted Auditing Standards (GAAS). The purpose of an audit is to provide an objective independent examination of the financial statements. The aim is to increase the value and credibility of the financial statements produced by management, thus increase user confidence, reduce investor risk, provide reliability and consequently reduce the cost of capital. An important objective in financial reporting is to provide information that will aid external users in decision-making. However, this information is expected to be readily available in a short interval of time from the end of the reported period, otherwise, it loses some of its economic value”. Timeliness therefore becomes an important characteristic of financial accounting information for prompt decision making. It can also be seen as a means of decreasing information asymmetry, mitigating insider trading and reducing the chances of spreading rumors about the firms’ financial health and performance (Al-Ajmi, 2008; Soltani, 2002).

Timeliness is seen as a qualitative attribute of general purpose financial reporting. “Presentation of financial information in a timely fashion is about making audited annual report and account available to the users of financial information as and when due and ensuring that it is current when it is received and when it is to be used as information”(Accounting Principle Board, 1970).The timeliness of submitting audit reports can increase the usefulness of the information produced (Deni, 2018). The longer the time for submission, the lower the economic value. The delay in submitting audited annual reports can trigger a delay in stock transactions by potential shareholders, which can cause investor distrust of the company. Timeliness reflects the credibility and quality of the information presented. The longer the delay period for the issuance of audit reports, the more the relevance and reliability becomes increasingly doubtful.

There is need for empirical studies in the industrial goods firms in Nigeria particularly on the subject of financial leverage and audit report timeliness and its attendant effect on the economy. Previous studies so far on this subject such as Azubike and Aggreh (2014), Arowoshegbe, Uniamikogbo and Adeusi (2017), Ohaka and Akani (2017), do not have a coverage period extended to 2018 and none of them used this sector of the economy. Thus, this is the gap that this work will fill.

Timeliness of audit report is of immense importance to all the stakeholders of industrial firm such as the management, the shareholders and potential investors in a number of ways; timely audited financial report will help management of firm to prepare budget, it also makes it easy to take appropriate financial decisions that leads to firm growth and also improves the financial management of the firm by helping to examine and correct any weaknesses in the financial systems. Timely audit reporting helps in performance evaluation to assess the performance of the Employees in the financial performance of the firm (Ramotar, 2017). The study also has the ability to educate potential investors of industrial goods firms to be more aware of the importance of timeliness of audit reporting and the need for companies to publish annual reports on time to enable them make informed decision. In the same vein, it could also serve as a basis for the formulation of laws and policy implementations. For example, Company and Allied Matters Act (CAMA, 1990 as amended) and SEC could recommend penalties for companies which fail to comply with the duration stipulated for their annual audited accounts to be made public.



The objective of this work is to examine the effect of financial leverage on timeliness of audit reporting of listed industrial goods firms in Nigeria. To achieve the specific objective of the research, a null hypothesis has been formulated and tested in the study:

H₀: Financial leverage has no significant effect on timeliness of audit report of listed industrial goods firms in Nigeria.

The research covered a period of seven years from 2012 to 2018. The study is structured into five sections: section one is the Introduction, section two takes up the literature review, section three presents the methodology, section four deals with results and discussions and section five concludes the study.

2. Literature Review

Conceptual Issues

Leverage, also referred to as gearing, is a relationship existing between assets and liabilities of a firm. In other words, it is the total debts employed by a firm to finance its assets. Leverage can also be used as a measure of the firms' ability to repay their financial obligations as they mature. Firms with larger debts than equity are viewed as highly leveraged and involve extensive auditing time and require high standard auditing services through the hiring of highly qualified auditing firms, thereby sustaining greater agency and monitoring costs. Afterwards, managers of greatly leveraged companies are inclined to reducing costs by means of relating more information in their audited annual reports and accounts (Jensen & Meckling, 1976). Such organisations may most likely postpone the announcement of their audited annual reports and account (Che-Ahmad & Abidin, 2008; Al –Ghanem & Hegazy, 2011; Owusu-Ansah, 2014).

Leverage is considered as one of the commonly used indicators of a firm's financial health. It is also argued that a firm's debt structure has a significant impact on the effectiveness of the firms' internal control system, and the extent of financial misreporting and financial failure (Shin, Lee, Lee & Son, 2017). As an end result, auditors will be more skeptical about the trustworthiness of financial statements of firms with poor internal control systems that could be the result of high leverage and as such auditors could put in more auditing time to investigate authenticity of the debts. According to Khalid, Alkhatid and Qasis (2012) which is adopted as the operational definition in this study, financial leverage is a measure of total assets to total liability.

Timeliness of audit report on the other hand, is a measure of the interval of time amongst a firm's year-end and the date of release of financial information to the public. Jim (2014) opined that, "timeliness can be measured as the time between when data is expected and when it is readily available for use. It also means having information available to decision-makers in time to be capable of influencing their decisions. In general, the older the information is, the less useful it is. However, some information may continue to be timely long after the end of a reporting period because, for example, some users may need to identify and assess trends".

The timeliness of financial reporting has been defined from different perspectives. For instance, Carslaw and Caplan (1991) posited that, timeliness is where information is made available readily to users as fast as possible otherwise it is not timely. "Timeliness is the period between the company's year-end and the date that the financial report was released for public view. Similarly, timeliness is making the financial information available to users on time so as to



influence their decision. Information given at the right time has more impact and usefulness than when it is made available after decision had been made. In the same vein, the Conceptual Framework for Financial Reporting (2010) identified timeliness as one of the four characteristics of useful information (McGee, 2007; International Accounting Standard Board, 2008).

Consequently, financial report timeliness is about making sure that financial data gets to the targeted users on time providing them with appropriate and valuable information for decision making process. Timeliness can be defined as the ability of decision makers to have access to information before it loses its importance and ability to affect judgments (Arowoshegbe, Uniamikogbo & Adeusi, 2017). For example, giving out accurate, excellent and comprehensive business information for more than one year-end is not as appropriate as delivering less comprehensive and complete financial statement in a few months after year- information is not available as and when due but rather made available so late that it bears no value for future action, then it is operationally irrelevant. To fulfill their primary objective and be useful, therefore, financial reports are expected to be characterised by relevance, reliability, completeness, and timeliness” (Ohaka & Akani, 2017).

In general, the lesser the time lag, the more effective the decision one can make out of it. However, Davies and Whittred (1980) as cited in (Salem, 2013) opined that the concept of timeliness in financial reporting has two dimensions. First is the frequency of reporting and the length of reporting period. There is also the lag between the end of the reporting period and the date the financial statements are issued. In the same way, Enarsson (2006) stated that there are two aspects of timeliness in financial reporting. One is the frequency of the reports while the other is the delay from the accounting date of the report to the date of the report’s release. In this study, timeliness is concerned with the second aspect of the delay in the issue of financial statements to users.

Theoretical Review

This work is anchored on agency theory because of the business association that exists between the agent and the principal taking into consideration the problem (conflict of interest) which exists between them that hinders the agent from carrying out his responsibilities and facilitate information asymmetry, thus, resulting in audit report lag. Agency theory originated from the study of Berle and Means (1932). They examined the agency concept and the applications toward the development of large corporations. The study found out how the interest of the directors and managers differ from the owners of the firm, hence using the conceptions of agency-principal to explain the origin of those conflicts.

Jensen and Meckling (1976) advanced the work of Berle and Means (1932) to develop agency theory as a formal concept. They also posited that, the agency relationship is a contract under which one party (the principal) engages another party (The agent) to perform some service on their behalf. As part of this, the principal will delegate some decision-making responsibility to the agents. This theory points out the role of certain corporate governance mechanisms to reduce agency problems. “In this context outside board of directors could strengthen the firm value by lending experienced and monitoring services and are supposed to be guardians of the shareholders’ interests through monitoring and control this is because greater proportion of



outside directors could monitor any self-interest by managers and so minimize agency costs” (Fama & Jensen, 1983).

“A high percentage of independent directors on board could intensify the monitoring of managerial opportunism. In so doing, they succeed in reducing management’s chance of withholding information (in a timely manner). Consequently, a board dominated by independent non-executive directors who are free from management interests tend to enhance firm’s compliance with disclosure requirements, which may lead to timely financial reporting. Preparers of accounts tend to sacrifice the reliability of information by focusing largely on timeliness, because lack of timeliness may cause information to have zero usefulness for decision making and/or information available from other sources” (Kelton & Yang, 2008; Ohaka & Akanni, 2017). The late information then results in poor allocation of capital, even as outside investors and creditors are subjected to adverse choice and moral hazards (Leventis & Weetman, 2004). Where there is less separation of power and control, timeliness of information is still crucial to creditors and external shareholders.

“A component of the agency costs is represented by the monitoring costs supported by shareholders for the monitoring of the managers actions. Since it is not acceptable to publish financial statements unless a certified public accountant (external and internal auditor) first audits them, the external audit effort is an important component of these costs, as long as auditors have to make sure that managers act according to the shareholders’ interests, while also auditors have the required task to inspect the accounts of the company. It may hence be supposed that auditors will spend more time inspecting the managers’ activity and therefore increase timeliness if there are agency problems. In actual fact, the agency relationship between the managers and shareholders may cause the agency conflicts to occur, thus corporate governance is assumed to be the best monitoring and controlling mechanism to reduce such problems. In relation to financial reporting and audit timeliness, corporate governance mechanism may reduce the audit business risk of the company; therefore reduce the audit work and hours taken by the auditor to complete their annual audit work” (Jensen & Meckling, 1976; Azubike & Aggreh, 2014).

Accounting and Auditing are the essential factors in monitoring agency relationship. Healy and Palepu (2001) view financial reporting and disclosure as most sought after because of the problems of information lopsidedness and the conflicting interests of managers and outside shareholders. Auditing has an important role to play in terms of monitoring agency contracts. This is because auditing role has a correlation with both information asymmetry and conflicts of interests. This theory assesses those problems that may occur between the agent and the principal such as conflict of interests and management problems which might lead to audit reporting lag.

Empirical Review

A number of empirical studies have been carried out to analyse the effect of financial leverage on timeliness of audit reporting. In respect to studies conducted locally in Nigeria, Efobi and Okougbo (2014) explored the factors that can influence the timeliness of financial reporting in Nigeria using a sample of thirty-three (33) financial institutions listed in the floor of the Nigerian Stock Exchange (NSE) for the period of 2005 to 2008. Eighteen (18) of which are



banks and fifteen (15) insurance companies. The Generalised Least Square (GLS) regression method was used for the estimation and the results revealed that leverage exhibit a negative significant effect on the timeliness of financial reports. The study used four years for analysis which this present study surpass. Similarly, Mohammed (2015) investigated the audit lag (i.e. time taken to complete the audit work) of Nigerian quoted companies, as listed on the Nigerian Stock Exchange for the period of 2012 to 2013. The research was conducted on a pooled sample of two hundred and sixty-six (266) firm-years across ten industries. Data collected was analysed using regression method. The result from the analysis showed that, leverage has significant effect in explaining audit lag. It was also revealed that companies with more leverage were found to be subject to longer audit work. This is perhaps due to auditors' being doubtful about the reported accounts.

Additionally, Adebayo and Adebisi (2016), investigated the timeliness of financial statements among the Deposit Money Banks in Nigeria. The study selected a sample of fifteen (15) Deposit Money Banks listed in the Nigeria Stock Exchange between 2005 and 2013. The data were analysed and results estimated using Ordinary Least Square (OLS) Regression accompanied by panel data estimation technique. The study established that leverage was not statistically significant and did not appear to have any bearing on financial reporting lag. A positive correlation between timeliness and leverage indicates that bank with high debt profile has significant reporting delay. The findings also revealed that most of the banks now comply with regulations which enhance timely reporting of financial statements in Nigeria.

On international scene, AL-Tahat (2015) examined the timeliness of half-yearly financial reports published by companies listed on the Amman Stock Exchange (ASE). The study also determined the association between leverage and timely reporting of the companies. An analysis of 193 half-yearly financial report of 30th June 2013 revealed that no significant association was evidenced between leverage and timeliness. This result may not however, show a true reflection of the effect of leverage on timeliness since it only analysed half-yearly result and not a full year result. Likewise, Hoang, Dang and Nguyen (2018) studied the factors affecting the timeliness of financial reports of enterprises in Vietnam. The research used panel data involving 1070 observations of companies listed on Vietnam's stock market covering the period of 2012 to 2016. The results was analysed using the Generalised Least Square (GLS) method which showed that financial leverage does not affect the timeliness of financial reports. The research results also showed that there are differences and statistical meanings in the publishing time of different types and starting times of financial reports.

Similarly, Surachyati, Abubakar and Daulay (2019) examined and analysed the influence of leverage on the timeliness of the submission of financial statements of the transportation companies listed on the Indonesia Stock Exchange. The population of the study was thirty (30) transportation companies listed in the Indonesia Stock Exchange covering the period of 2011-2015. Data was analysed using logistic regression through the use of Statistical Package for Social Sciences (SPSS). The study found that financial leverage variable has no significant effect on the timeliness of financial statement submission. Additionally, Enni and Raja (2019) evaluated the effect of leverage on the timeliness of financial report submissions of the 78 trade, services and investment companies listed in Indonesia Stock Exchange between the years 2014 to 2016. Multiple linear regression was used to test the hypotheses. The result of the study



showed that leverage does not have an effect on the timeliness of the submission of financial reports because leverage cannot be a guide in determining the extent of mandatory financial statement disclosures due to policy differences in each company. The empirical gap based on the review range from period covered, domain, statistical package, research design and the sources of data.

3. Methodology

The study used ex - post facto research design technique. The ex-post facto research design seeks to retrieve the study data for events which have before now occurred. It can also be referred to as “after the fact” research design because it’s a system in which groups that already existed are related on some dependent variables. Testing the validity and reliability of the data was considered unnecessary as the data has been published and thus seen as certified by external auditors. The population of the study comprised of 14 listed Industrial Goods Firms quoted in the Nigerian Stock Exchange (NSC). However, a purposive sampling technique was used to arrive at 13 firms. The study was carried out using secondary data sourced from annual reports for seven years covering the period of 1st January, 2012 to 31st December, 2018 obtained from NSE. The annual reports were collected from the various company’s websites.

Descriptive statistics is used to describe and summarise the behaviour of the variables in this study. Regression analysis was used find out the effect of Financial Leverage on Audit Report Timeliness. Data collected was analysed using Stata. The Procedure for Data Analysis and Model Specification is as stated below:

The independent variable for this study is leverage (LEV), “computed as the ratio of total leverage (short term debt + long term debt) to total asset of the company”.(Khalid, Alkhatid & Qasis, 2012).The dependent variable which is Timeliness (TML) or Audit Delay also called Reporting Time Lag or Interim Period, “measured by the interval between the last day of accounting year and the date of auditors’ signature”(Modugu, Eragbhe & Ikhatua, 2012; Oladipupo & Izedomi, 2013; Akingunola, Soyemi & Okunuga, 2018). A control variable is an element which is not changed throughout the cause of a research. It is unchanging, and because of this it allows the association between other variables being tested to be better understood. Hence, this study introduced one more item which is size of the company. The control variable Size of the Company (SZCOM) is measured as natural logarithm of yearend total assets (Shukeri & Islam, 2012; Ohaka & Akanni, 2017).

The model specification is as follows:

$$TML_{it} = \beta_0 + \beta_1 LEV_{it} + \beta_2 SZCOM_{it} + \epsilon \dots\dots\dots 1$$

Where:

- TML = Timeliness of Audit Report
- LEV = Leverage
- SZCOM = Size of the company (control variable)
- ε = Error Term
- β₀ = is the intercept
- β₁ - β₂ = is the parameter to be estimated in the equation
- i = Number of sample firms



t = Number of years

4. Results

This section presents data used for the study, analysis and discussion of findings in accordance with the specific objective of the research.

Descriptive Statistics

Table 1: *Descriptive Statistics*

Variable	Observations	Mean	Std.Dev.	Min	Max
TML	91	4.4746	0.2284	3.6109	5.1929
LEV	91	0.6831	0.1802	0.2024	1.2241
SZCOM	91	0.0011	0.0002	0.0005	0.0016

Source: Researchers' Computation Stata 14.2

From Table 1, TML (Timeliness) is a dependent variable while LEV (Leverage) is the independent variable of the regression model. TML has an average mean of 4 months and 5 days for the industrial firms and is skewed towards the right since it is greater than the median with a minimum 3 months 6 days and a maximum lag of 5 months and 2 days which is more than 90 days as stipulated by SEC. This is an indication that many of the industrial companies exceed the stipulated period for the publication of their audited annual report.

LEV has a minimum value of 0.20 which implies that the company has the minimum capacity to pay back its debt at 0.20. The lesser the value of the company's leverage, the more timely it will be in submitting its audited annual report and accounts. However, the maximum value which the industrial firms indebted to as shown by the observation 1.22. The higher the amount of a firm's leverage, the more the company will be late in submitting its audit report (Surachyati, et al 2019). This points out that, the amount of leverage acquired by the firms range from between 0.20 to 1.22. The average value of leverage owed by the observed company is 0.1802. The standard deviation measures the average distance between each quantity and mean. From Table 1, it can be observed that data is well spread out from the means of TML and LEV having overall standard deviations of 0.228 and 0.180 respectively.

4.2 Regression Analysis

Tables 2 to 4 respectively present results of the ANOVA, over all Model Fit and the regression analysis with one dependent variable to be Timeliness (TML) and one independent variable to be Leverage (LEV) having Size of the Company (SZCOM) as a control variable.

Table 2: *ANOVA*

Source	SS	Df	MS
Model	0.5556	2	0.2778
Residual	4.1413	88	0.0470
Total	4.6969	90	0.0521

Source: Researchers' Computation Stata 14.2

Table 2 shows the analysis of variance in the outcome table as the categories to be looked at which are model (variance which can be explained by independent variables), residual (variance which is not explained by independent variables) and total. Sum of Squares (SS) associated with



the three sources of variance – Total, Model and Residual are respectively .5556, 4.1414 and 4.6969. Their degrees of Freedom (df) and Mean Square (MS) are also shown in the Table.

Table 3: *Over all Model Fit*

Number of obs	91
F (2, 88)	5.90
Prob> F	0.0039
R-squared	0.1183
Adj R-squared	0.0983
Root MSE	21694

Source: Researchers' Computation Stata 14.2

It can be seen from Table 3 that 91 observations were used in the regression analysis. The F-statistic which is the mean square model divided by the mean square residual is 5.90 with a p-value of 0.0039 which indicates that the model is statistically significant. The R-squared is 0.1183, which means that approximately 12% of the variability of TML is accounted for by the variables in the model. The adjusted R-squared indicates that about 10% of the variability of TML is accounted for by the model after taking into account the number of predictor variables.

Table 4: *Regression Analysis Result*

TML	Coef.	Std. Err.	T	P> t	95% conf.	Interval
LEV	0.4537	0.1377	3.29	0.001	0.1800	0.7273
SZCOM	-35.8233	93.9647	-0.38	0.704	-222.5586	150.9119
_cons	4.2053	0.1136	36.99	0.000	3.9793	4.4312

Source: Researchers' Computation Stata 14.2

From Table 4, the coefficient of the independent variable is 0.454 for LEV. This means, for every unit increase in LEV there will be an expected increase of 0.454 in TML all other variables being held constant. The estimated coefficient of the individual variables can be represented in the regression model as follows:

$$TML = 4.2053 + 0.4537LEV - 35.8234SZCOM$$

4.3 Discussion of Findings

The objective of this work is to study the effect of financial leverage on timeliness of audit report of listed industrial goods firms in Nigeria. The null hypothesis of the study states that:

H0: Financial leverage has no significant effect on timeliness of audit report of listed industrial firms in Nigeria.

From Table 4, the P>|t| column shows the 2-tailed p-values used in testing the null hypothesis that the coefficient is 0 using an alpha of 0.05. The coefficient of LEV is 0.454 which is statistically significant because its P-value of 0.001 is smaller than 0.05. From the estimates of the model, LEV has positive significant effect on timeliness of audit report of listed industrial goods firms in Nigeria. Based on the result, the null hypothesis which states that leverage has no significant effect on timeliness of audit report of listed industrial firms in Nigeria is rejected. It can therefore, be concluded that, we reject the null hypothesis and state that leverage has no significant effect on audit report timeliness of listed industrial firms in Nigeria. This outcome is



in line with the findings of Mohammed (2015) but contrary to the findings of Adebayo and Adebisi (2016); Surachyati, Abubakar and Daulay (2019).

5. Conclusion and Recommendations

Extremely leveraged firms involve extensive auditing time and high standard auditing services through the hiring of qualified auditing firms with such auditors putting in more time to investigate authenticity of the debts with managers of such companies obligated to relate more information in their audited annual reports and accounts which may lead to delay in timely reporting. This work therefore, examined the effect of financial leverage on timeliness of audit reporting of listed industrial firms in Nigeria covering the period of 2012 to 2018. Data was sourced from annual report and accounts of the companies. Multiple regression analysis was employed, the study found that there is a positive significant effect of LEV on TML of listed industrial firms in Nigeria. Based on the findings, it is recommended that industrial firms should not desist from having huge amount of debt to finance their investment as this will reduce the audit time lag. Further research on audit report timeliness should be done using other variables.

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