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AUDIT COMMITTEE AND INTEGRITY OF FINANCIAL STATEMENTS: A Preventive Mechanism for Corporate Failure.

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ABSTRACT

Corporate governance is a phenomenon that has recently attracted local and foreign interest due to the frequent occurrences of corporate failures experienced by various organizations in both developed and developing nations around the world. Financial statements are the midpoint of this corporate disorder and auditing profession is said to responsible for the disaster. This has brought the question of how efficient is our financial system and the effectiveness of the audit infrastructure. This study investigated the effect of audit committee oversight function on integrity of financial statements as a means preventing organizational failure. The population of this study consisted of 183 public quoted companies in the Nigerian Stock Exchange, 100 medium and large audit firms and 616 investor with about 10% holding in PLC. Data was elicited using structured questionnaires. Hypotheses were confirmed using Z-test. The result shows that there is significant relationship between audit committee activities and integrity of financial statements, which enhances the quality corporate governance and prevents organizational failure. The study recommended that a committed audit committee should be established and members to be appointed should possess analytical skill with strong financial background. The will go a long way to curb the incessant corporate failure in Nigeria.

Keywords: *Corporate governance, Agency theory, Audit committee, Financial statements, Corporate failure*

1.0 INTRODUCTION

The emergence and development of public limited liability companies brought changes in ownership structure and a complete divorce between ownership and management. Professional managers designated Directors are employed as “agents” to manage the business affairs on behalf of shareholders called principals. This separation becomes necessary due to professionalism, cutthroat competition and complexity in contemporary management (Broadley, 2006). This new wave in corporate management gave credence to business operations and investors confidence that resources placed at the disposal of professional managers are well-utilized (Uzuh, 2006). Physical absence of shareholders in the business and given the amount of resources invested makes it not only necessary but also mandatory for Directors to render stewardship accounts to members of the company at least annually S 334(1) of CAMA 1990. Uzuh (2006) stated that unsuccessful management may window-dressed the financial statements to hide the cause of their failure hence government legal provisions to protect investors by enacting laws that an independent person known as the “Auditors” should carry out audit test on the on financial statements and supporting documents. The audit test will enable the Auditors report his opinion to the members of the company on the true and fairness of the financial statements prepared by the directors (S. 357(1) of CAMA 1990). The auditor’s examination of financial statements provides assurance and reduces investment risks and uncertainty, which aids users in making informed economic decisions (Broadley, 2006). The concept of governance and the responsibilities for integrity of financial statements procedures lie with Board members. This is supported by a formal structure of corporate governance mechanism (Gwilliam & Marnet, 2006).

The aim of establishing audit committee is to overhaul the financial system and uphold the integrity of the financial statements to reflect economic substance of transactions and present a true and fair view (Ojo, 2006). Auditors, who are indirect stakeholders, are blamed by the public for the failure of most organizations on the ground that financial statements of a company with a going concern issues had unqualified report. The issue of auditor’s involvement has raised the following questions: (i) do the auditors play any key role in corporate governance? An attempt to resolve the above question generated two alternative situations when the functions of auditors and the requirements of good corporate governance are matched against one another. The former is restricted to economic actions and events, while the later is the product of a wide range of managerial functions (ii) The second question is whether the auditors should cross their operational limits in order to bring about the desired level of improvement in the quality of governance or should they restrict themselves to their term of reference in accordance the law (Brennan, 2006). Naveen & Singh (2012) noted that corporate board is the zenith of internal corporate governance mechanism**.** Board of Directors are entrusted with the role of

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monitoring management, ensuring effective internal controls and protecting the rights of shareholders (Jensen & Mecking, 1976). The research question on which the study attempts to provide answer includes (i) To what extent has audit committee's activity improve the integrity of financial statements? (ii)Does quality of financial statements improve good corporate governance and prevents corporate failure? The hypotheses of the study are: H_{o1}: Integrity of financial statements does not depend on role Audit committee in an organization and H_{o2}: Good corporate governance does not prevent organizational failure.

2.0 REVIEW OF RELATED LITERATURE

According to Rwegasira (2000 as cited in Oyejide & Adedoyin, 2001) corporate governance as a concept can be examination from at least perspectives: the narrow and broad. The narrow viewed the concept as being concerned with the structures within which a corporate entity receives its basic orientation and direction while the broad perspective regards corporate governance as being the heart of both a market economy and a democratic society (Sullivan, 2000). This research will be limited to the narrow view to enable corporate governance be treated in terms of issues relating to shareholders protection, management control and the popular principal-agency problems of economic theory. Cadbury Committee (1992) defined corporate governance as the system by which companies are directed and controlled. Central Bank of Nigeria (2006) noted that "good corporate governance" is a system by which corporations are governed and controlled with a view to increasing shareholder value and meeting the expectations of other stakeholders. OECD (2004) noted that corporate governance comprehends that structure of relationships and corresponding responsibilities among a core group consisting of shareholders, board members and managers designed to best foster the competitive performance required to achieve the primary objective. The above definitions maintained a good level harmony but were not able to relate to financial system of an organization. A more comprehensive definition is that of The Toronto Stock Exchange (1994). Corporate governance is seen as a process and structure used to direct and manage the business and affairs of the corporation with the objective of enhancing shareholder value, which includes ensuring the financial viability of the business. It also stated that the process and structure describes the division of power and establish mechanisms for achieving accountability among shareholders, the board, and management. Wilson (2006) added that corporate governance is about the manner in which corporations are directed, controlled, and held to account for the resources used. The obligation of public trust for companies to act in a manner that protects the public interest and make full and fair public disclosure of corporate information including financial results since they raised funds from the public and serves as the basis for corporate governance (Inyang, 2009).

2.1 Agency Theory

The term Agency Theory is a relationship that subsists when one person or group of persons called agent is acting on behalf of another called principal. This theory arises due to the possible conflict of separating ownership from day to day management of organization (Oye, 2010). It addresses in particular the principal-agent relationship between shareholders and directors on the one hand and the relationship between company agents and stakeholders on the other (Hayes, et al 1999). According to Hill and Jones (2001), corporate governance could mean the mechanisms used to govern managers and ensure that their actions are consistent with the interests of key stakeholder groups. In large companies, the shareholders involvements are restricted in practical terms hence monitoring function becomes vital due management deviations. This may give rise to pursuing personal interest at the expense of shareholders (Hillman and Dalziel, 2003).Sometimes manager of companies pursue other strategies than those selected by the board of directors to maximize shareholders returns because most of the time they are motivated by the desire for status, power, job security, and income. Corporate governance essentially focuses on the dilemmas that result from the separation of ownership and control.

2.2 Brief of History of Corporate Governance

The history of corporate governance is traced to the practice of preparing fraudulent financial statements by company directors and the auditors reporting along same manner in some developed countries. Corporate governance issues were critically reviewed after the collapse of Enron and WorldCom in the U.S. and the fallout from Maxwell, BCCI, Polly Peck and others in UK. This led to the enactment of the Sarbanes-Oxley (SOX) Act No. 404 of July 2002 signed into law on July 30, 2003 in USA. The advanced western world saw the need to restore public confidence and the reputation of the accounting profession on which its franchise is based on integrity and accuracy and corporate governance was the answer. Sarbanes-Oxley (SOX) Act was designed to reform the accounting industry, restore investors' confidence and addresses the conflicts of interests, ensures auditor accuracy in their opinion on financial report and establishes safeguards to protect against investment analysts conflicts (Oyejide & Adedoyin, 2001). The new trends in corporate governance affected Africa's emerging markets (Osaze, 2007). Solomon (2007) noted that the origin of corporate governance in Nigeria is

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traced to the promulgation of the Companies and Allied Matters Act (CAMA) 1990 that replaced Companies Act 1968 as well as the following events: (i) In 1997, the cases of the 26 liquidated banks motivated the development of standards for corporate governance. In 2001, the Atedo Peterside committee set up by the Securities and Exchange Commission (SEC) identified weaknesses in the corporate governance practices in public companies and made recommendations to address them. A survey by SEC reported in 2003 revealed only 40% compliance by quoted companies including banks (SEC, 2003). Nmehielle and Nwauche (2004) revealed that a good compliance level with basic structural requirements of corporate governance such as size and composition of the board of directors, notice of annual general meetings, and others are in place (ii) A major move by the CBN was in 2006, in the development of corporate governance in Nigeria, when it issued the Code of Corporate Governance for Banks Post Consolidation sought to address the issues of corporate failure and create a sound banking system in Nigeria. Hayes et al (1999) identified among other issues the major cause of current corporate failure as bankruptcies, fraud, and mismanagement. The main objective of corporate governance is to make capital markets safer and investor-friendly by adopting best international business and accounting practices to protect investors and empower shareholders to provide greater value to their holdings. This will ensure entity's growth and stakeholders' prosperity. Osaze (2007) stated that the challenge of corporate governance is to find a way to maximize wealth creation overtime, in a manner that does not impose inappropriate costs on third parties or on the society as a whole.

2.3 Financial Statements and Auditing

Financial statements are reports of financial performance of the organization with respect to funds made available by owners and other providers of funds. S334(2) of CAMA 1990 states that subject to (3), of the section, the financial statements required under subsection (1) of this section shall include: (a) statement of accounting policies (b) the balance sheet as at the last day of the year (c) a profit and loss account or in the case a company not trading for profit, an income and expenditure account for the year (d) notes to accounts (e) the auditors reports (f) the directors reports (g) a statement of the source and application of fund (h) a value added statement for the year (i) a five year financial summary and (j) in case of a holding company, the group financial statements. It is the basis of the above statements that stakeholders' makes informed economic decisions but unfortunately, most financial statements of public quoted companies in Nigeria do not reflect the economic substance of the company financial position. Financial statements can be adequately relied upon by their users where a structure of review and authorization are put in place to enhance the integrity of such report.

This structure should contain procedures to ensure truthfulness and factual presentation of the company's financial position. According to ICAN (2006), the structure should include a process that ensures the independence and competence of the external auditors and the audit committee that reviews and consider the financial statements to enable the provision of confidence, reduces uncertainty and risk and adds value. The International Auditing Practices Committee (IAPC) of the International Federation of Accountants (IFAC) stated that the objective of audit of financial statements is to enable the auditor to express an opinion whether the financial statements are prepared in all material respects and in accordance with an identified financial reporting framework or other criteria. Broadley (2006) stated that apart from expressing opinion, the role of the auditor include looking for misstatements caused by either fraud or error that cause the financial statements not to present fairly the position of the company. The auditors seek to determine the strength of organization's internal control system (ICS) to enable reliance and performance of compliance test or otherwise substantive (Eilifsen et al, 2006). ICS a tool employed by management to prevent and detect irregularities and fraud, which is role of management. However, the auditor is expected to have knowledge of the client's systems and control in order to determine the appropriate audit strategy (Adeniji, 2004).

2.4 The Role of Audit Committee and integrity of financial statements

An audit committee according to S 350 (4) CAMA 2004 C20 LFN is an operating committee of the Board of Directors charged with oversight responsibility of financial reporting and disclosure. The committee members are drawn from the board with a chairperson selected from among the committee members. In U.S.A, the role of audit committees continues to evolve based on the Sarbanes-Oxley Act of 2002 and involves oversight of regulatory compliance and risk management activities, overseeing the financial reporting and disclosure process, monitoring choice of accounting policies and principles, overseeing hiring, performance and independence of the external auditors, oversight of regulatory compliance, ethics, and whistleblower hotlines, monitoring the internal control process, overseeing the performance of the internal audit function and discussing risk management policies and practices with management. In Nigeria, in response to the dynamic environment, Boards of Directors are now placing increasing reliance on audit committees to oversee reporting and internal control (Akinsulire, 2010). S 350 (3) CAMA 2004 C20 LFN the Auditor in addition to report made under

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subsection 1, of this section, shall make report to the audit committee, which shall be established by the public company. In Ss 4, the composition of the audit committee shall consist of equal number of independent directors and representatives of shareholders to a maximum of six numbers and members shall be subject to re election annually. Its responsibilities include examination of the auditor's report and making recommendation thereon to the annual general meeting as it think fit. According S.359 (6) CAMA 2004 C20 LFN, subject to such additional functions and power that the company's articles of association may stipulate, the objectives and functions of audit committee shall be to: (a) Ascertain whether the accounting and reporting policies of the company are in accordance with legal requirements and agreed ethical practices (b) Review the scope of planning of audit requirements (c) Review the findings on management matters in conjunction with the external auditors and departmental responses thereon (d) Keep under review the effectiveness the company's system of accounting and IC (e) Make recommendation to the Board in regard to appointment, removal and remuneration of the external auditors (f) Authorize the internal auditor to carry out investigation into any activities of the company which may be of interest to the committee.

Throughout the year, the audit committee learn and inquire about significant matters affecting financial statements and implement them. The committee benefits are (i) assist in establishing and strengthening the independence and objectivity of the directors and the internal and external auditors (ii) there will be improved communication and increased contact, understanding and confidence between directors, management and the internal and external auditors (iii) increased internal and external auditors' accountability as their performance are under greater scrutiny (iv) help to create a climate of discipline and control which reduces the opportunity for fraud (v) Result in efficient and effective external audit and (vi) strengthening the objectivity and credibility of financial reporting. For proper discharge of duties, all members of the committee should be financial literate and have understanding of the industry in which the company operates and at least one member have financial expertise and professional qualification of the recognized professional accounting bodies. When the audit committee carries out their responsibilities properly, the result is definitely a credible financial statements which is the basis for good corporate governance and corporate failures will be avoided.

3.0 METHODOLOGY

The population of this study consisted of 899 members distributed as 183 public quoted companies in the Nigerian Stock Exchange, 615 investors who meet the requirement of 5% holding in the public limited liability company and 100 Auditing firms in Nigeria. The sample size is determined by Yaro-Yeme's formula as stated below:

$$n = \frac{P}{1+\left[P(S)^2\right]}$$

Where; n = Sample size sought; p = 899, 1= Constant figure (given), $(S)^{2} = (5\%)^{2}$ or $(0.05)^2$ (usually assumed). Solving for the sample size (n): n= 899/ 1+ $[899(0.05)^2]$, n= 899/ 1+ [899(0.0025)] n= 899/ 1+ [3.2475)] n= 899/ 5.7475. **n = 277**. The researcher decided to use a census survey of all auditors on the ground that they are in the centre of corporate mess and are blamed by the public for every failure experienced in any company. 1 copy of questionnaire was administered to the Managing Partner of each audit firm while 177 copies of the questionnaire were administered to company directors (41) and shareholders (136) at random in the ratio of 22.15%. Data were collected from Respondents using multiple-choice structured questionnaires. The instrument was a 15-term survey questionnaire with a 5 Likert scale response as follows: High, Medium, Low, No influence, and No Opinion. In order to convert the ordinal scale to Interval Scale, a weighting was given to each point in the 5-point Scale 4-0 in the descending order. Hypotheses of the study were confirmed using Z test. The Z distribution designated as 'Z' was used as the test statistic on the ground that the sample size is large (>30). The parametric test statistic is represented by the following formula:

$$\mathbf{Z} = \frac{\mathbf{X_1 - X_2}}{\sqrt{\frac{\mathbf{S_1 + S_2}}{n_1 + n_2}}}$$

Where $\mathbf{X_1}$ = mean of the first sample or group**;** $\mathbf{X_2}$ = mean of the second sample or group; $\mathbf{S_1}$ = variance or standard deviation of the first sample or group; $\mathbf{S_2}$ = variance or standard deviation of the second sample or group; n_1= number of the observation or sample size of the first sample; n2 = number of the observation or sample size of the second sample. The **Decision rule is (**i) Reject Ho if Z calculated > Z critical value (ii) Otherwise do not reject. The level of significance of the study is 5% or 0.05 level. Thus, the probability is 0.05that a true null hypothesis will be rejected.

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4.0 TEST OF STATISTICAL THE HYPOTHESIS

4.1 Table 1: Summary of hypotheses test results

Variable / Group	HN	X	SD	n	df	SE	Cal. Z Value	Crit. Z Value	Remark
Directors / Shareholders	1	3.35	0.824	170	268	107	8.224	$\pm$1.96	Reject Null Hypothesis
Auditors		2.47	0.852	100					
Directors / Shareholders	2	3.35	0.824	170	268	107	6.204	$\pm$1.96	Reject Null Hypothesis
Auditors		2.47	0.852	100					

Source: Field work – November, 2012

Interpretation key: X= means, SD= Standard deviations, n = number of the observations, SE = Standard errors, df = degree of freedom, HN= Hypothesis Number.

Decision: Hypothesis 1 -Since the Z calculated value of 8.224 > the critical value of tabulated Z value of $\pm$1.96, we reject the hull hypothesis (H_0) and accept alternate hypothesis (H_1). This suggests that there is a significant relationship between Audit committee and integrity of financial statements. This relationship is proved by 92 Director and Shareholders on point 4 while 13 auditors on point 4. Hypothesis 2 - Since the Z calculated value of 6.204 > the critical value of tabulated Z value of $\pm$1.96, we reject the hull hypothesis (H_0) and accept alternate hypothesis (H_1). This suggests that there is a significant relationship between corporate governance and organization failure. This relationship is confirmed by question 7 with 131 and 53 high responds to rank first

5.0 THEORETICAL FINDINGS

This study was carried out to investigate whether, in the context of corporate governance, audit committee plays an important role in making financial statements a report of consequence, The results of the study shows that (i) audit of financial statements, attestation of internal control systems and internal auditing improve the corporate governance of an organization (ii) The integrity of financial statements of plc depends on the degree of audit committee's activities (iii) The incessant organizational failure can reduced to the barest minimum if financial statements reflects the economic substance of business transactions

6.0 CONCLUSION AND RECOMMENDATIONS

The study has demonstrated that despite the strong roles played by external auditors in an organization, the role in audit committee cannot be compromised promoting corporate governance. Despite the fact that an independence auditors should carry out the audit of public limited liability companies, there should check and balance and this can only done through establishment of committed audit committee of the Board of Directors. The results of the study also showed that audit committees activities improves corporate governance of an organization through the audit of financial statements, establishing and reviewing the internal controls and improving on the accounting policies adopted. The result shows that there is significant relationship between audit committee activities and integrity of financial statements, which enhances the quality corporate governance and prevents corporate failure. The study recommended that a committed audit committee should establish and members to be appointed should possess the analytical skill with strong financial background. The will go a long way to curb the incessant corporate failure in Nigeria

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Appendix 1

Test of statistical hypotheses

Table 2: Summary of Questionnaire Distributed and Respondents

RESPONSES	ADMINISTERED	PERCENTAGE	VALID RETURNED	PERCENTAGE
Directors / Shareholders	177	64%	170	63%
Auditors	100	36%	100	37%
Total	277	100%	270	100%

Source: Field work – November, 2012

Hypothesis 1

H_o: Integrity of financial statements does not depend on role Audit committee in an organization

H_1: Integrity of financial statements depend on role Audit committee in an organization.

Table 3: Summary of responses for Directors / Shareholders and Auditors: Question 12 Does integrity of financial statements depend on the activities of Audit committee in an organization

Options	Level of Audit Committee's Influence on Financial Statement					
	High (4)	**Medium (3)**	**Low (2)**	**Influence (1)**	**No Opinion (0)**	**Total**
Directors / Shareholders	92	52	20	6	0	170
Auditors	13	32	44	11	0	100
Total	**105**	**84**	**64**	**17**	**0**	**270**

Source: Field work – November, 2012

Computation of Means and Standard Deviations

Table 4: Computation of Means for **Directors / Shareholders and Auditors**

Options	Point (x)	Directors / Shareholders		Auditors	
		Resp. (f)	**Fx**	**Resp. (f)**	**Fx**
H	4	92	368	13	52
M	3	52	156	32	96
L	2	20	40	44	88
NI	1	6	6	11	11
NO	0	0	0	0	0
Σ		**170**	**570**	**100**	**247**
Mean X			**$X_1 = \Sigma fx = 570/170 = 3.35$**		**$X_2 = \Sigma fx = 247/100 = 2.47$**

Source: Field work – November, 2012

Table 5: Computation of Standard Deviations for **Directors / Shareholders and Auditors**

Point (x)	Directors / Shareholders				Auditors			
	Resp.	**$X - X_1 = X_{v1}$**	**$F(X_v)$**	**$F(X_v)^2$**	**Resp.**	**$X - X_1 = X_{v2}$**	**$F(X_v)$**	**$F(X_v)^2$**
4	92	0.65	92(0.65)	38.87	13	1.53	13(1.53)	30.43
3	52	-0.35	52(-0.35)	6.37	32	0.53	32(0.53)	8.99
2	20	-1.35	20(-1.35)	36.45	44	-0.47	44(-0.47)	9.72
1	6	-2.35	6(-2.35)	33.135	11	-1.47	11(-1.47)	23.77
0	0	-3.35	0(-3.35)	0	0	-2.47	0(-2.47)	0
Σ	**170**			**114.83**	**100**			**72.91**
SD				$S_1 = \Sigma f(x_1)^2/N-1 = 114.83/170 - 1 = $ **0.679** $SD_1 = \sqrt{S_1} = \sqrt{0.679} =$ **<u>0.824</u>**				$S_1 = \Sigma f(x_2)^2/N-1 = 72.91/100 - 1 = $ **0.736** $SD_2 = \sqrt{S_2} = \sqrt{0.679} =$ **<u>0.852</u>**

Source: Field work – November, 2012

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Computation of Z Value

The data for the computation of Z Value are: X_1= 3.35; X_2 = 2.47; SD_1 = 0.824; SD_2 = 0.852; N_1 = 170; N_2 = 100

$$Z = \underline{X_1 - X_2} / \sqrt{\frac{S_1 + S_2}{n_1 + n_2}}$$

$$Z = 3.35 - 2.47 / \sqrt{\frac{0.824^2 - 0.852^2}{170 + 100}} = 0.88/ / \sqrt{0.0004+0.0074} = 0.88/ / \sqrt{0.0114}$$

= 0.88/ / 0.107 Standard error. **Z calculated = <u>8.224</u>**

Using the degree of freedom df = 268, and 0.05level of significance or 5% of probability Z – calculated is equal to Z_{268} (0.05) = $\pm$1.96 since this is a two tailed test and we are not concerned with the direction of variance.

Table 6: Test comparison between Directors / Shareholders and Auditors on influence of Audit committee on integrity of financial statements in a Public limited liability company.

Variable / Group	X	SD	n	df	SE	Cal. Z Value	Critical Z Value	Remark
Directors / Shareholders	3.35	0.824	170	268	107	8.224	$\pm$1.96	Reject Null Hypothesis
Auditors	2.47	0.852	100					

Source: Field work – November, 2012

Decision: Since the Z calculated value of 8.224 > the critical value of tabulated Z value of $\pm$1.96, we reject the hull hypothesis (H_0) and accept alternate hypothesis (H_1). The suggest that there is a significant relationship between Audit committee and integrity of financial statements. 92 Directors and Shareholders proved this relationship on point 4 while 13 auditors on point 4.

Hypothesis 2

H_o: Good corporate governance does not prevent organizational failure

H_1: Good corporate governance prevents organizational failure

Table 7: Summary of responses for Directors / Shareholders and Auditors: Question 7 Good corporate governance prevents organizational failure

Options	Level of Audit Committee's Influence on Financial Statement					
	High (4)	**Medium (3)**	**Low (2)**	**No Influence (1)**	**No Opinion (0)**	**Total**
Directors / Shareholders	131	29	6	4	0	170
Auditors	43	19	35	3	0	100
Total	**174**	**48**	**41**	**7**	**0**	**270**

Source: Field work – November, 2012

Table 8: Computation of Standard Deviations for **Directors / Shareholders and Auditors**

Point (x)	Directors / Shareholders				Auditors			
	Resp. (f)	**X- $X_{1=}$ X_{v1}**	**$F(X_v)$**	**$F(X_v)^2$**	**Resp. (f)**	**X- $X_{1=}$ X_{v2}**	**$F(X_v)$**	**$F(X_v)^2$**
4	131	0.31	131(0.31)	12.59	43	0.98	43(0.98)	41.30
3	29	-0.69	29(-0.69)	13.81	19	-0.02	19(-0.02)	0.01
2	6	-1.69	6(-1.69)	17.14	35	-1.02	35(-1.02)	36.41
1	4	-2.69	4(-2.69)	28.94	3	-2.02	3(-2.02)	12.24
0	0	-3.69	0(-3.69)	0	0	-3.02	0(-3.02)	0
Σ	**170**			**72.48**	**100**			**89.96**
SD	$S_{1} = \Sigma f(x_1)^2/N-1$ = 72.48/170 -1=**0.429** $SD_1 = \sqrt{S_1} = \sqrt{0.429}$ = **<u>0.655</u>**				$S_{1} = \Sigma f(x_2)^2/N-1$ = 89.96/100 -1=**0.909** $SD_2 = \sqrt{S_2} = \sqrt{0.909}$ = **<u>0.953</u>**			

Source: Field work – November, 2012

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Computation of Z Value

Data for the computation of Z Value are: X_1= 3.69; X_2 = 3.02; SD_1 = 0.655; SD_2 = 0.953; N_1 = 170; N_2 = 100

$$Z = \underline{X_1 - X_2} / \sqrt{\frac{S_1 + S_2}{n_1 + n_2}}$$

$$Z = 3.69 - 3.02 / \sqrt{\frac{0.655^2 - 0.953^2}{170 + 100}} = 0.67 / \sqrt{0.0025+0.0091} = 0.67 / \sqrt{0.0116}$$

$$= 0.67 / 0.108^{-} \text{ Standard error.} \quad \textbf{Z calculated = 6.204}$$

Using the degree of freedom df = 268, and 0.05level of significance or 5% of probability Z – calculated is equal to Z_{268} (0.05) = $\pm$1.96 since this is a two tailed test and we are not concerned with the direction of variance.

Table 9: Test comparison between Directors / Shareholders and Auditors on influence of Audit committee on integrity of financial statements in a Public limited liability company.

Variable / Group	X	SD	n	df	SE	Cal. Z Value	Critical Z Value	Remark
Directors / Shareholders	3.35	0.824	170	268	107	6.204	$\pm$1.96	Reject Null Hypothesis
Auditors	2.47	0.852	100					

Source: Field work – November, 2012

Decision: Since the Z calculated value of 6.204 > the critical value of tabulated Z value of $\pm$1.96, we reject the hull hypothesis (H_0) and accept alternate hypothesis (H_1). This suggests that there is a significant relationship between corporate governance and organization failure. This relationship is confirmed by question 7 with 131 and 53 high responds from Directors /Shareholders and Auditors to rank first.