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Financial Reporting Quality and International Financial Reporting Standard (IFRS) Adoption in Nigeria

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Abstract

The study aims to determine how financial reporting quality of Nigerian enterprises relates with International Financial Reporting Standards (IFRS). The study adopted the descriptive statistical design, the study sample is made up of 14 listed deposit money banks (DMBs) listed in Nigeria Exchange. Secondary data were extracted from those companies for both pre and post IFRS era in Nigeria. The study found that IFRS affects the financial reporting quality of Nigerian Stock Exchange-listed companies. Before and after IFRs, financial statements meant different things. Financial statements under Pre-IFRS and Post-IFRS were equally reliable. The research recommends that the Financial Reporting Council (FRC) promote IFRS adoption in Nigeria through aggressive awareness initiatives. To increase IFRS awareness, expertise, and use, regulatory and professional bodies should finance field-specific training.

Keywords: *Financial Reporting Quality, International Financial Reporting Standard*

1. Introduction

The degree to which financial reports offer accurate, pertinent, comprehensible, verifiable, and objective information regarding the fundamental financial status and financial performance is known as financial reporting quality (Bala et al., 2018).High-quality financial reporting is essential for decision-making and resource allocation in companies, protecting users from poor investment choices and enhancing capital market efficiency. Global comparability of financial reports is also crucial for maintaining a favorable balance of trade. Financial reporting standards vary by region, regulated by different bodies. For instance, In the United States, it is overseen by the Financial Accounting Standards Board (FASB), but there are differences between countries, such as between the United Kingdom, the United States, Japan, and emerging markets (Masoud, 2017).

To bridge this gap, the International Financial Reporting Standards (IFRS) were established. IASC provides international accounting standards for recording and reporting business transactions and required disclosures (Desalegn, 2020). The goal of adopting IFRS is to improve the global consistency, clarity, and usefulness of financial statements. IFRS are standards based on principles,

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establishing global rules and detailed accounting guidelines (Adetiloye et al., 2016; Aboud & Roberts, 2018; Adetiloye et al., 2016).

Before adopting IFRS, Nigeria had its own accounting standards, Created by the Nigerian Accounting Standards Board (NASB), this was referred to as the Statement of Accounting Standards (SAS). The alignment of SAS with IFRS was approved on January 1, 2012. In June 2011, The Financial Reporting Council of Nigeria (FRCN) replaced NASB and assumed responsibility for overseeing the adoption and implementation of IFRS. The transition began in September 2010, with a mandate for all listed companies and significant public interest entities to adopt IFRS by January 1, 2012. Public sector organizations had until January 2013 to comply, while small and medium-sized enterprises (SMEs) were granted an extension until January 2014. As the global adoption of IFRS continues to grow, ensuring the reliability and transparency of financial reporting has become an increasingly important issue. In developing countries like Nigeria, the financial statements of both listed and unlisted companies affect a broad spectrum of stakeholders. The integrity of these statements is particularly important in today's globalized economy. IFRS was adopted in Nigeria to ensure uniform standards and high-quality financial reporting). Financial reporting is only useful if it is relevant, comparable, understandable, and reliable. Poor-quality financial statements can lead to economic breakdowns and capital market collapse, particularly in developing countries like Nigeria.

This study investigates the perceived solutions offered by IFRS adoption in addressing these issues in Nigeria and the challenges faced in achieving high-quality reporting.

2. Literature Review

2.1 International Financial Reporting Standards

International Financial Reporting Standards (IFRS) consist of worldwide accounting principles that outline the transactions and events to be included in financial statements. They state how accountants have to keep and document their records (Alawiye-Adams 2018). These standards aim to achieve consistency by standardizing reporting practices. IFRS enables the creation of comparable financial statements across different jurisdictions. They also achieve understandability by defining reporting methods to enhance clarity and facilitate comprehension of financial information for users like investors and creditors.

2.2 IFRS Adoption in Nigeria

On September 2, 2010, Nigeria adopted the International Financial Reporting Standards (IFRS). This move aimed to enhance Nigeria's competitive position in the global economy and reap the benefits of IFRS adoption. Following the Federal Executive Council's (FEC) approval, a schedule for IFRS implementation starting in 2012 was devised. Before adopting IFRS, The Nigerian Accounting Standards Board (NASB) introduced the Statement of Accounting Standards (SAS), which was based on Nigerian GAAP and aligned with IASB standards. Established in 1982 and formally recognized by Act No. 22 of 2003, which became law on July 10, 2003, the NASB played a key role in accounting regulations. In 2011, the Financial Reporting Council of Nigeria (FRCN) was created, and the Financial Reporting Council of Nigeria Act was enacted, signifying the shift to IFRS. This Act abolished the NASB Act of 2003. Prior to the formation of the FRCN, the FEC had already outlined a plan for IFRS implementation in Nigeria, with specific timelines for reporting:

Entities with substantial public interest and those listed on public exchanges: By January 1, 2012, these companies had to compile their financial accounts using IFRS. Their closing balances as of December 2010 had to be converted to IFRS-based values, which would be starting from January 1, 2011, the initial IFRS financial statements were required to be presented for the year ending December 31, 2012.

Additional Public Interest Organizations: By January 1, 2013, all other entities with public interest were required to adopt IFRS for legal reporting purposes.

Small and Medium-Sized Enterprises (SMEs): By January 1, 2014, SMEs Organizations were mandated to prepare financial statements based on IFRS for the year ending December 31, 2014. At present, private sector companies in Nigeria are required to follow IFRS. For the public sector, the International Public Sector Accounting Standards (IPSAS) are the applicable standards. IFRS, along with the International Accounting Standards (IAS), which were initially issued by the

International Accounting Standards Committee (IASC), form the complete framework of IFRS in use today.

2.3 Financial Reporting

Financial reports summarize a business's financial situation and organize accounting data. Lauren Oliver (2022) describes financial reporting as recording and sharing information on financial activity and performance over specific intervals, typically quarterly or annually. Effective financial reporting is structured, easy to understand, and includes basic financial statements with management analysis (KPMG, 2013). Cheung, Evans, and Wright (2010) highlight key characteristics for financial statements:

Understandability: Information must be clear to users, as supported by standard-setting bodies like the IASB and FASB. **Comparability:** Users should be able to recognize similarities and differences between financial statements, requiring consistency in their preparation. **Reliability:** Information must be reliable to be useful, with credibility of audited reports being crucial for different users.

2.4 Nigerian Financial Reporting in the Pre-IFRS Era

Traditionally, Nigerian financial statements followed generally accepted accounting standards (GAAP), which provided the framework for recording transactions. These local GAAPs were tailored to Nigeria's specific political, cultural, legal, and economic contexts. Before adopting IFRS, the Companies and Allied Matters Act of 1990 governed financial statement format, content, disclosure requirements, and auditing, mandating compliance with Nigerian Accounting Standards Board (NASB) guidelines.

2.4.1 Financial Reporting in the Post-IFRS Era

Since adopting IFRS in 2012, Nigerian financial reporting has improved, aligning with global standards and enhancing transparency and comparability. Abdulkadir Madawaki (2019) notes significant differences between IFRS and NG-GAAP in areas such as equity changes, income statements, management estimates, property, plant, equipment, related parties, segment reporting, leases, damage disclosure, risk management, financial guarantees, consolidation scope, and employee benefits.

2.4.2 Benefits of IFRS Adoption in Nigeria

Adopting IFRS in developing countries like Nigeria offers numerous benefits, as highlighted in several Nigerian studies. According to Oladeji and Agbesanya (2019), the benefits of IFRS adoption include:

Transparency and Comparability: IFRS improves financial statement transparency and comparability, enabling Nigerian companies to present operations more clearly. **Enhanced Accountability:** IFRS reduces the information gap between capital sources and investment beneficiaries, providing regulators with comparable information globally. **Flexibility:** IFRS's principle-based approach allows Nigerian companies to adapt standards to their circumstances, leading to more readable and useful financial statements. **Foreign Investment:** Adherence to IFRS can boost investor confidence, enabling Nigerian firms to raise capital in international markets at lower costs. **Economic Efficiency:** By helping investors to spot worldwide prospects and risks, IFRS helps to improve capital allocation and lower foreign reporting costs for Nigerian companies.

2.5 Theoretical Review

2.5.1 Positive Accounting Theory

Positive accounting theory, as discussed by Makassar (2020), aims to explain why different firms and accountants use various accounting methods. It includes three hypotheses: political cost, debt covenant, and bonus plan. William H. Beaver introduced this theory in 1968 with his essay "The Information Content of Annual Earnings Announcements" (Jensen & Meckling, 1976). The theory seeks to both forecast and explain accounting principles, clarifying why businesses change their accounting methods and continue using historical practices.

2.5.2 Legitimate Theory

According to legitimacy theory, companies try to make sure their operations fit society expectations and limitations (Deegan et al., 2002).Closely related to stakeholder theory, it falls within the political economy theory framework (Rahmawati, 2012; Gary, Kouhy, & Lavers, 1994). Our study is anchored on this theory.

2.5.3 Value Relevance Models

This approach evaluates the consistency, relevance, productivity, and variability of financial information. The Value Relevance Model examines the relationship between accounting data and stock market responses to the integrity of financial reporting (Nicholas & Wahlen, 2004). A strong correlation suggests that earnings information is relevant and reliable, while accounting data show the market value of the company depending on accounting practices, stock prices reflect it.

3. Methodology

Among the numerous research designs, this study adopted the descriptive statistical design, deemed most suitable for its purposes. Descriptive statistics are techniques used to calculate, summarize, and present research data in a clear and efficient manner.

The study's population includes public liability corporations from various sectors such as banking, oil and gas, brewing, construction, and cement. A random sample of 14 firms from the Nigerian Exchange, specifically from the banking sector, was selected. This study relies on secondary data, specifically financial statements from selected Nigerian banks.

3.1 Model Specifications

The model for this study was adopted from Kythreotis (2014). The study's model on the impact of IFRS adoption on value relevance is presented as follows: EM = $=\beta_o+\beta_1 IEit_1+\beta_2 IFRS+\beta_3 E$ $\hat{}IFRS_3+\beta_4 SIZEit+ \beta_5 MB_{it} +\varepsilon it$.

The model is modified to suit our study thus:

Model 1: Measuring Relevance before and after the adoption of IFRS

IFRS$SPji=a0+a1BVit+a2EPSji+a3CFOa+a4ACCit+eji$

Model 2: Measuring Reliability before and after the adoption of IFRS

$CFOiT+1=a0+a1BV+a2EPSit+a3CFOit+a4ACCit+eit$

Where:

$SPitSPit$ = Share price of firm, ii in year tt.

$BVitBVit$ = Book value of equity of firm, ii in year tt.

$EPSitEPSit$ = Earnings per share of firm, ii in year tt.

$CFOit+1CFOit+1$ = Cash flows from operating activities in year, $t+1t+1$.

CFOitCFOit = Cash flows from operating activities of firm, ii in year tt.

ACCitACCit = Accruals (Working Capital - Depreciation) for firm ii from year $t-1t-1$ to tt.

Parameters estimates (a0,1,2,a3,a4a0,a1,a2,a3,a4) and the error term (ee) are included in these models.

4. Results and Discussions

Descriptive Statistics for Testing the Significance, Relevance and Trustworthiness of financial statements before and after the adoption of IFRS.

Hypothesis One, Two, and Three

The descriptive statistics of the variables comprising the model are compiled in the table below. SP (Share Price), used as a proxy for Relevance, has a mean of 17.16 ± 8.32 in the Pre-IFRS period and 38.41 ± 7.22 in the Post-IFRS period. CFOT (Cash Flow from Operations), a proxy for Reliability, shows a mean of 1.82E+11 ± 1.82E+11 in the Pre - IFRS period and 185189800.0 ± 167925527.7 in the post-IFRS period.

The skewness values indicate that all variables were positively skewed in the pre-IFRS period. In the post-IFRS period, all variables remained positively skewed except for ACCR (Accruals), implying a subtle connection between accruals and cash flow throughout this period.

Table 4.1: Pre-IFRS and Post-IFRS Descriptive statistics

Period T		Variables	Mean +SD	Skewness
Pre-IFRS	Relevance	SP	17.16± 8.32	1.37
		EPS	198.80 ± 113.56	1.25
		BV	15.17± 7.31	1.21

	Reliability	CFOT	1.82E+11 ± 1.82E+11	0.92
		CFO	1.05E+11 ± 1.02E+11	0.82
		ACCR	7.57E+10 ± 7.93E+10	0.82
Post-IFRS	Relevance	SP	38.41 ± 7.22	0.65
		EPS	118.78 ± 78	2.24
		BV	31.70 ± 6.39	0.70
	Reliability	CFOT	185189800.0 ± 167925527.7	0.37
		CFO	130562000.0 ± 139075287.9	0.87
		ACCR	142030600.0 ± 105454305.9	-0.286

Researchers output 2024.

4.3 Paired T-test Comparing the Difference in the Relevance and Reliability of Financial Statements before and after the adoption of IFRS.

Table 2 illustrates a notable change in the relevance of financial statements before and after IFRS adoption ($p=0.005$). However, no significant variation was found in the reliability of financial statements before and after IFRS implementation ($p=0.09$).

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Table 4.2: Paired t-test analysis of the differences and reliability of financial statements before and after the adoption of IFRS

	Mean	Std. Deviation	T	P
Relevance	-21.26	8.69	-5.468	0.005
Reliability	1.81E+11	1.82E+11	2.224	0.09

Researchers output 2024

Hypothesis Testing

Hypothesis One: The review of previous literature in chapter two and three and the paired T-test shows the significant influence of IFRS on the reporting quality of financial statements in the post-IFRS era.

Hypothesis Two: There is significant difference in the relevance of financial statements in Nigeria before and after the implementation of IFRS.

Test: **Paired** **t-test**

Alpha level: 0.05

Observed p-value: 0.005

Judgment: Since the observed p-value is less than 0.05, the null hypothesis is REJECTED.

Hypothesis Three: There is no major change is observed in the reliability of financial statements in Nigeria prior to and following the adoption of IFRS.

Test: **Paired** **t-test**

Alpha level: 0.05

Observed p-value: 0.09

Judgement: Given that the observed p-value exceeds 0.05, the null hypothesis is accepted. This study identified three key findings:

a) The quality of financial reporting for companies listed on the Nigerian Stock Exchange is heavily influenced by IFRS.
b) The implications of financial statements changed significantly before and after IFRS adoption.
c) There was no significant difference in the reliability of financial statements before and after the implementation of IFRS.

5. Conclusion and Recommendations

The importance of adopting IFRS as the main standard for financial reporting in Nigeria is crucial. This is due to the enormous benefits derivable from such adoption by companies in particular and the economy in general. Although the adoption of IFRS in Nigeria may not yield all its anticipated benefits, it will help in solving some issues as regards financial reporting in Nigeria to a large extent. It is therefore necessary that some of the challenges associated with its adoption in Nigeria be resolved so that companies implementing it and the economy as whole will start reaping the advantages of Nigerian adoption of IFRS.

To this end, the following suggestions have become necessary;
The Financial Reporting Council (FRC) should promote IFRS adoption in Nigeria through aggressive marketing. To improve IFRS awareness, knowledge, and implementation, regulatory bodies and professional groups should finance field-specific training programs. Regulators should be financially supported to ensure firms obey IFRS. Companies should also assist in ensuring that their staff members get the required training on IFRS adoption because they stand to gain in the long run. The government should ensure IFRS acceptance and application in Nigeria by creating the appropriate conditions. They can do this by providing the necessary legal foundation for acceptance and application.

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