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Analysis of Financial Reporting Quality among Firms in Nigeria

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Abstract:
The study analysed the quality of financial reporting among firms in Nigeria to determine the level of compliance of selected firms with relevant regulations governing the preparation and presentation of published financial reporting. Secondary data were used for this study, and a total of 112 firms listed on the Nigerian stock exchange that were non-financial companies, out of which 50 whose published financial statements were up to date, were selected using a purposive sampling technique. Data were obtained from the Nigerian Stock Exchange and the selected firms' websites.
Descriptive analysis was used to analyse the data using percentages and tables.
The results showed a significant improvement in the quality of financial reports among firms in Nigeria, ranging from 0.706 in 2008 to 0.8072 in 2018.
The study concluded that the quality of financial reporting among firms in Nigeria was high.

Keywords: *Financial reporting, quality, listed non-financial firms*

1. Introduction

Every listed company in Nigeria is compelled by law to publish its annual reports for the public and interested users' consumption. Financial reporting is the reporting system that encompasses the report of an enterprise's activities in quantitative and qualitative terms. It is a statement comprising information about the effects of transactions and other events that change the reporting entity's economic resources and claims. The income and changes in the economic position of that company are shown for a particular period. The information contained in the financial report should be useful, relevant, and have faithful representation. The useful information can be seen to assist in the determination of economic decision-making by the shareholders. Relevant information will also assist the users in making economic decisions because the information may be able to determine what happens to the future investment's value. Faithful representation means the information is complete, neutral, and free from error. The importance of quality financial reporting to various stakeholders cannot be over-emphasized in decision-making. The concept of financial information states that the primary objective of financial reporting is to avail the diverse users of financial information, such as equity holders, potential investors, lenders, and other stakeholders, of the required information that would ease their economic decision process in investing and providing to the entity. Normally financial reports based on sound financial reporting standards were obtained by analysts and were free from misstatement. This information can then be used in the assessment of the performance of the organization. However, in practice, financial reporting can either be high-quality with complete and accurate accounting information or low-quality with misleading, inaccurate, and incomplete financial information. The great lacuna in the financial reporting system led to a high financial scandal which led to both losses of confidence and loss of investment by investors. The financial report contains items that are indicators that can be used to examine the financial performance of the entity discovered that the state of financial reporting in Nigeria was found to be weak because the information left out of the report is vital, according to Wallace, 1988, Adeyemi, 2006, Nzekwe, 2009. The information left out is the information that can be of assistance for investment for investors. The World Bank also researched the disclosure practices in which the corporate financial reporting is weak, which was an affirmation of earlier submission. There are a lot of benefits derivable from the provision of reliable and complete information on the activities of the enterprise. Benefits in the form of a reduction in the level of information risks associated with poor quality of reported information that may prevent investors from being able to make investment decisions. It also reduces the information gap created by the agency relationship conflict (Rajgopal & Venkatachalam, 2011). Jo and Klim (2007) stated that companies that give a higher quality of financial reporting are in a position to give a global outlook of the transactions of the business to investors of the company to make better and informed decisions. It is because they have good information at their disposal. In addition to financial reports, the auditor also prepares the Domestic/Management Report, which will show the in-depth analysis of the accounts reported on by the audit firm. However, this report is only made available to the management and audit committee. So many issues raised in the domestic report shall be discussed at a joint meeting. The joint meeting is made up of management, auditors (internal and external), and the audit committee. The domestic report will address some critical issues that will make the financial report free of misstatement. Such issues like the assessment of the procedure for the appointment of staff into key positions, the procedure for procurement and sales, the inventory system, the banking system, and adequate record keeping. The work of the internal auditor will also be examined to know whether they can rely on the accounts presented by management for audit. The auditor will want to be sure whether they are following various regulations in carrying out the assignments of the organization. All the observations will be highlighted, the effects will also be mentioned, and recommendations will be made to the management for necessary action. The management will have to react to all the issues raised by the auditor and how they want to go about it. It is either the management who came out with explanations or agreed to make necessary corrections. If there is an area where the company is doing well, it will be reported, and recommendations will be made for the company to still improve on that. The auditor will always review the previous year's management report to know whether actions have been taken on issues raised in the last audit. After the auditor is satisfied, the annual report will be signed and presented for board approval. If these procedures are duly followed, the financial report will be free from misstatement and bias. Financial Reporting contains qualitative and quantitative information analysis, as shown in the annual report. For the financial information to be realistic, it must, therefore, satisfy certain criteria before it could be considered useful to stakeholders. The financial information can be assessed through the following as established in the Conceptual Framework for Financial Reporting (2018): such as Relevance, Reliability, understandability, comparability, Consistence, Neutrality, materiality, Timeliness, Verifiability and substance over form. The form of the financial report of each firm may differ due to information asymmetry.

2. Literature Review

The essence of financial reporting is to satisfy or bridge the information gap between the principal and the agents. The users of financial reports vary with varying interests, so the information should be prepared and presented to the users for decision-making.

The relationship between two parties involved in a contract which consists of a principal as the party given the responsibility of a task and an agent as the party who delivers the responsibility, is what is termed to be an agency relationship (Adman M, 1994). A contract by which one or more persons (the principal(s)) contract another person (the agent) to execute some service in favor of them and which involves delegating to the agent some authority of decision-making is also an agency relationship (Meckling, 1976).

The agency relationship goes beyond shareholders' and managers' relationship but also includes the relationship between debenture holders/managers, creditors/managers, clients/managers, and government/managers. This relationship results in a consequence that parties, agents, and principals will try to maximize their utility.

There are reasons mentioned under agency theory that make it so important, and this includes but is not limited to the remoteness of the stakeholders. The stakeholders may be far away from the management, which has created an information gap. The auditor, as an agent, will close this gap by communicating effectively with the stakeholders through the audit report. There is also a complex situation that will need somebody to analyse the conviction of the stakeholders. The transactions may be so complex that they may not be understandable by the stakeholders unless the agent can communicate through a fair presentation of the economic realities. In addition, the management may have a conflict of interest and thereby may not be able to present the information adequately; the agent will now do this. Furthermore, the consequence of financial misstatement may be damaging to the stakeholder, and this can lead to a loss of investment on the part of the stakeholders for relying on unreliable information. The auditor, as the agent, is in a position to forestall this problem. This study is based on the agency theory.

3. Methodology

The study used descriptive analysis to interpret the secondary data collected. The quality of financial reporting of listed non-financial firms in Nigeria was assessed based on the specific recommendation of the relevant and identified financial reporting frameworks such as IAS and IFRS. Inconsistent with this reporting framework and the recommendation, this study constructed a general reporting quality index representing the overall disclosure of required information in Nigeria and ranked the listed firms in Nigeria. Accordingly, the data used to develop the composite quality index were extracted from financial reports filed by Nigerian firms to the Nigeria Stock Exchange. The required disclosures were captured by the construction and design of the quality index.

The frequency distribution consists of 50 listed non-financial firms on the Nigerian stock market whose stocks were traded on Nigerian Stock Exchange from 2008 to 2018. This represents all firms with available data that were adequate to carry out the required analysis during the sample period. The frequency distribution indicates no clustering in any specific year, as demonstrated in table 1 below. The data is a balanced panel with annual data, and the observation includes firms in the sample if a firm has its shares traded at least once a year and also was financial data in the year. The study also shows the distribution of firms by the industry as defined by Nigeria Stock Exchange.

Year	No of Firms	Percentage of Sample
2008	50	100
2009	50	100
2010	50	100
2011	50	100
2012	50	100
2013	50	100
2014	50	100
2015	50	100
2016	50	100
2017	50	100
2018	50	100

Table 1: Distribution of Firms by Year
Source: NSE Fact Book Publication 2018

Industry	No. of Observation	Percentage of Sample
Health Care	7	0.14
Agriculture	2	0.04
Construction	6	0.12
Consumer Goods	13	0.26
ICT	3	0.06
Industrial Goods	5	0.10
Natural Resources	2	0.04
Oil and Gas	5	0.10
Services	4	0.08
Conglomerate	3	0.06
	50	1.00

Table 2: Sample Breakdown by Industries
Source: NSE Fact Book Publication 2018

4. Discussion of Results

The study analyzed the quality of financial reporting of listed non-financial firms in Nigeria. The analysis is done in line with the disclosure requirements and was based on the analysis of the annual financial statements, which contain accounting information. The analysis was done by developing a reporting quality index (RQI) to measure the firms' quality of reporting and analyze the extent of compliance and adherence of firms to the minimum disclosure requirements as prescribed by relevant financial reporting frameworks, particularly the International Financial Reporting Standard. Since 2002, firms worldwide have been required to adopt International Financial Reporting Standards (IFRS). The essence was to promote quality and uniformity in preparing and presenting accounting information that would serve the economic need and investment interests of various users of financial accounting reports. The disclosure of required and necessary information is expected to enhance the quality, ensure greater comparability and transparency of accounting information and reduce information asymmetry. Therefore, this study analyzed the quality of financial reports or statements of firms that have already adopted internationally recognized standards and used available disclosure quality scores extracted from a detailed analysis of annual reports by reputed accounting scholars (experts). This work complements other contemporary research on the quality of financial statements where earnings properties are used as an evaluation metric.

The analysis shows, on average, a significant improvement in the quality of financial reports. Even though there is an obvious indication that quality varies across firms and industries, the differences are not materially significant.

Table 1 shows the quality of financial reporting among firms in Nigeria, and the Financial Reporting Index is measured on a scale of 0 to 1. The closer to zero the RQI, the lower the financial Reporting quality, and the closer to 1 the RQI, the higher the financial reporting quality. Undoubtedly, all the sample firms complied with the disclosure requirements of the accounting standards and demonstrated high financial reporting quality during the sample period. There is an improvement in the scoring average of RQI from 0.70611 in 2008 to 0.8072 in 2018. The highest recorded values of financial reporting quality within the period under study ranged from 0.8602. to 0.8201. On average, the study shows a financial reporting quality score of 0.763912, representing about 76.3% which is high and suggestive of gradual improvement in the quality of financial reporting.

Firm	Financial Reporting Quality
Glaxo smith cline Consumer Nigeria plc	0.8602
Omateck ventures Plc	0.8583
Forte oil plc	0.8583
Pz Cussons Nigeria Plc	0.8465
Chams Plc	0.8201
First aluminum Nigeria plc	0.8201
Nigerian Breweries Plc	0.8162
Morison Industries Plc	0.8098
Dangote Cement Plc	0.8055
Oando Plc	0.8055
UAC Nigeria Plc	0.8055
May & Baker Nigeria Plc	0.7996
Guinness Nigeria Plc	0.7996
Academy Press Plc	0.7977
John Holt Plc	0.7977
Scoa Nigeria Plc	0.7977
Okomu Oil Plc	0.7967
Flour Mills Nigeria Plc	0.7957
Evans Medical Plc	0.7956
Ag Leventis Plc	0.7879
Vita Foam Nigeria Plc	0.7879
Dangote Sugar Brewery Plc	0.7869
Nemeth International Pharmaceuticals Plc	0.7774
Lafarge Africa Plc	0.7774
Champion Brew Plc	0.7722
Julius Berger Nigeria Plc	0.7693
Portland Paints and Products Plc	0.7595
Triple Gee and Company Plc	0.7565
Conoil Plc	0.7565
Roads Nigeria Plc	0.7555
Beta Glass Nigeria Plc	0.7555
Fidson Medical Plc	0.7554
Japaul Oil and Maritime Services	0.7537
Cadbury Nigeria Plc	0.7535
Union Dicon Salt Plc	0.7429
Berger Paints Nigeria Plc	0.7429
Thomas Wyatt Nigeria Plc	0.7429
Pharma Deko Plc	0.7388
Multiverse Mining and Exploration Plc	0.7388
Unilever Nigeria Plc	0.7367
Arbico Plc	0.7322
Chellarams Plc	0.6997
Nestle Nigeria Plc	0.6865
Honeywell Flour Mills Plc	0.6851
Ftn Cocoa Processing Plc	0.685
NCR Nigeria Plc	0.6813
Total Nigeria Plc	0.674
Smarts Products Nigeria Plc	0.6635
Northern Nigeria Flour Mills Plc	0.6489
International Breweries Plc	0.605

Table 3: Financial Reporting Quality Index
Source: Author's Computation, 2020

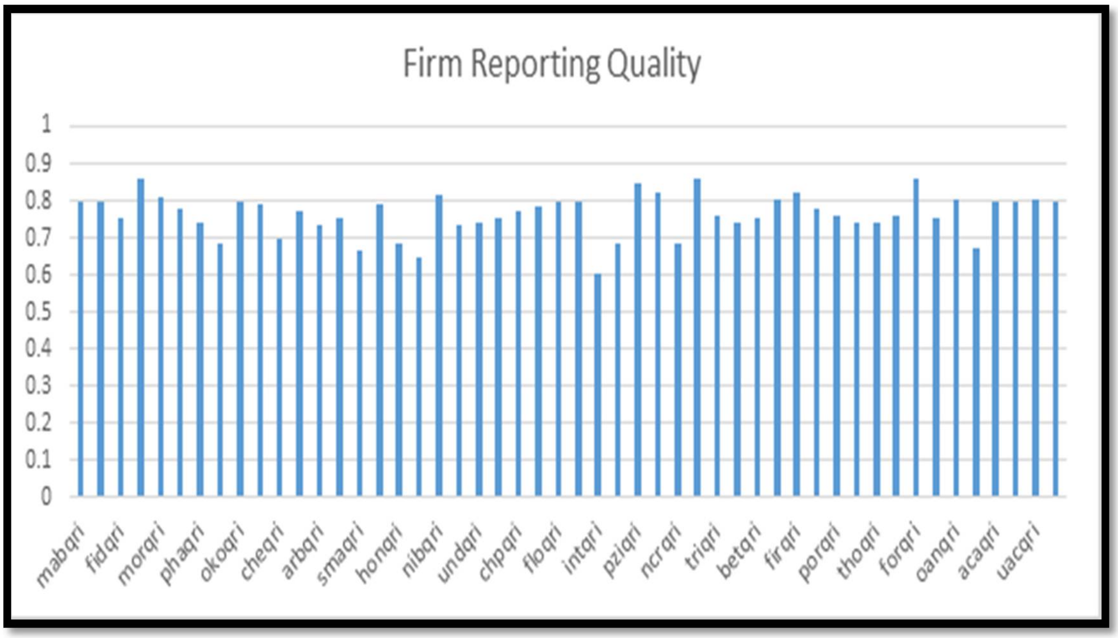

Figure 1: Firm Reporting Quality
Source: Author's Computation, 2020

The study further analysed the trend and changes in the quality index. This is shown in table 2 and figure 1. The trend of annual financial reporting quality across the sample firms in Nigeria showed upward and downward variations in the RQI index score. The reporting quality index score, which stood at 0.706 in 2008, rose to 0.722 in 2009 and dropped to 0.7219 in 2010. The decline continued in 2011 and 2012 with values of 0.7194 and 0.7770, respectively. However, there was an upward shift in 2013 as the score rose to 0.7906 and kept increasing till 2015 with an index score of 0.7924. In 2016, there was a slight and insignificant drop in quality to 0.7740, but in 2017 and 2018, it rose to 0.8053 and 0.8072, respectively.

The fluctuation in the quality index score may not be unconnected with changes in management and the attendant corporate governance risk. There is no doubt that improved financial reporting Quality is expected with the presence of corporate governance**.** The differences and the decline rate, though very mild and far from extreme, may be due to different management philosophies. The presence of this key factor, that is, management changes which have been argued as a determinant factor in the financial reporting process, is evident and common among firms and is capable of causing a breakdown in the financial reporting process (Bala, Amran & Shaari, 2018; Al-Rassas & Kamardin, 2015). Compliance with financial reporting frameworks requires management's complete adherence to the corporate governance code and other regulations governing the activities of the business within the industry. Thus, a sound management system reduces misstatements in the financial report. Thereby, the management and other various players in the governance process, particularly external and internal auditors, play a key role in ensuring and influencing the attainment of financial reports that are free from material misstatements and misrepresentations. The analysis of the quality of financial reporting shows that listed firms in Nigeria ensure that information required by applicable financial reporting standards is disclosed in their financial reports to provide adequate, relevant, and timely financial information to the users.

Year	Average Financial Reporting Quality
2008	0.70611
2009	0.7225
2010	0.7219
2011	0.7194
2012	0.7770
2013	0.7906
2014	0.7854
2015	0.7924
2016	0.7740
2017	0.8053
2018	0.8072

Table 4: Trend of Average Financial Reporting Quality
Source: Author's Computation, 2020

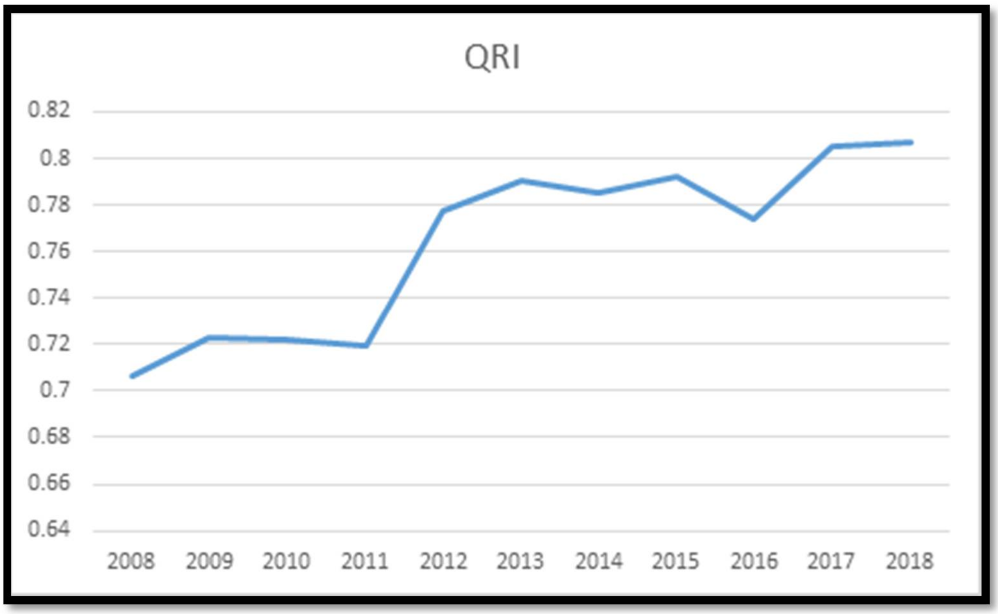

Figure 2: Trend of Financial Reporting Quality
Source: Author's Computation, 2020

5. Conclusion

The results showed that the sample firms demonstrated a high level of financial reporting, which indicates that the sample firms complied with statutory regulations in respect of disclosure requirements. The result ranges from 0.862 to 0.820 between 2008 and 2018. Though there is an obvious indication that quality varies across firms and industries, the differences are not materially significant.

The study, therefore, concluded that the quality of financial reporting of listed non-financial firms in Nigeria is very high.

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