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RESEARCH PAPER

INTERNATIONAL FINANCIAL REPORTING STANDARDS AND FINANCIAL REPORTING QUALITY IN NIGERIA

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ABSTRACT
The study examines the impact of the adoption of International Financial Reporting Standards (IFRS) on the quality of financial reporting in Nigeria. The study utilises a period based approach to analyse changes in the degree of financial reporting quality (FRQ) that hinges on three proxies: Value Relevance, Earnings Quality and Earnings Management. Three models were developed to capture each proxy, and the models were analysed using regression analysis to evaluate the R^2 statistics; which captured the direction of change in the reporting quality. The results showed that financial reporting quality increased after the adoption of the IFRS for all the relevant proxies. The study concludes that the adoption of IFRS to enhance financial reporting quality while reducing the probability of earnings management practices could be beneficial in the long run to the Nigerian financial landscape.

Keywords: *Reporting Standards, Value, Relevance, Earnings, Management*

INTRODUCTION
The need for uniformity of financial statements across borders led many economies to adopt the International Financial Reporting Standards (IFRS). International Financial Reporting Standards are issued by the International Accounting Standards Board (IASB), an independent organisation registered in the United States of America (USA) but based in London, United Kingdom. IASB issues financial reporting standards that ideally would apply equally to financial reporting by public interest entities worldwide. In Nigeria, adoption of IFRS was launched in September 2010, by the Honorable Minister, Federal Ministry of Commerce and Industry, Senator Jubril Martins-kuye. The adoption was organised such that all stakeholders would use the IFRS by January 2014 (Madawaki, 2012).

The IASB in its objectives and preamble, expects the beneficial effects from IFRS adoption to include transparency, improved accounting quality and reduced cost of capital. Despite the perceived benefits of the implementation of the IFRS, the adoption is wrought with challenges. These benefits and challenges could lead to favourable/adverse implications at both the micro and macro-economic levels. It becomes an interesting source for stakeholders to ascertain whether the standards are achieving their basic tenets and objectives. For instance IFRS is perceived to engender improvements in financial reporting quality due to increased stringency in its usage and application, and one wonders if this is really the case. It is also argued that implementing IFRS enhances earnings quality by reducing information asymmetry, decreasing earnings management, providing more value relevant financial information to investors/shareholders, and decreasing cost of capital.

Based on these assumptions, the study applied accounting quality measures; value relevance, earnings quality, and earnings management to find out whether the adoption of IFRS has led to improvements in the reporting quality of companies listed on the Nigerian Stock Exchange.

LITERATURE REVIEW

Previous research on the subject matter has produced differing results on the impact of IFRS on financial reporting quality. The effect of adoption of IFRS on financial reporting quality could vary across different countries. The mixed findings documented in earlier studies can be explained by countries' institutional structures. Many studies argue that developing and transitional economies still have ineffective institutions and infrastructure; though their capital market may be developing fast. Nigeria is one of the largest developing countries in Africa, characterised by concentrated ownership structures, weak legal systems and highly politicized institutional arrangements. These peculiarities could inform a level of variance in the results obtained in the study.

IFRS adoption and value relevance

IFRS adoption is generally encouraged because it is perceived to promote fair value accounting which inadvertently weakens the link between taxation and accounting rules, hence, it is expected that earnings and book value would automatically become more value relevant. However, extant literature on the implications of IFRS adoption on the value relevance of financial information has presented contentious views and results.

The empirical works of Muller (2014), Kargin (2013), Palea (2013), Lin *et al.* (2012), Karampinis and Hevas (2009) and Paglietti (2009) investigated the association between IFRS adoption and value relevance and they indicated that value relevance of accounting information improved during the post-IFRS period. The studies of Garanina and Kormiltseva (2013) and Outa (2011) however negated the positive effect of IFRS adoption on the value relevance of accounting information.

IFRS adoption and earnings quality

Ismail *et al.* (2013), Sellami and Fakhfakh (2013), Assidi and Omri (2012) and Sun *et al.* (2011) noticed increases in earnings quality in the post IFRS periods. However, the works of Ames (2013), Nullah (2013) and Hoque *et al.* (2012) showed that earnings portrayed lower persistency and predictability after IFRS adoption. Their studies generally stipulate that IFRS adoption *per se* does not lead to increased quality of earnings.

IFRS adoption and earnings management

The introduction of the IFRS has reduced the flexibility of accounting choices in the preparation of financial statements. The more stringent measures in the application of IFRS therefore led many to believe that the use of the standards would inadvertently lead to decreases in the propensity for earnings management. Also, the adoption of the standards is perceived to enhance the efficiency of the board of directors (due to the higher level of disclosure and transparency inherent in IFRS) which puts more constrain on them to monitor the extent of earnings management practices.

Athanasios *et al.* (2013), Dimitropoulos *et al.* (2013) and Iatridis and Rouvolis (2010) examined the impact of IFRS adoption on the quality of accounting information within the Greek accounting setting. They found convincing evidence that the implementation of IFRS contributed to less earnings management compared to the local accounting standards.

Liu *et al.* (2011) examined the impact of IFRS on accounting quality in China. Their empirical results generally indicate that accounting quality improved with decreased earnings management and increased value relevance of accounting measures. However Ahmed *et al.* (2013) in their meta-analysis found that discretionary accruals did not reduce post-IFRS adoption. Doukakis (2013) showed that IFRS adoption had no significant impact on either real or accrual based earnings management practices while the work of Jeanjean and Stolowy (2008) indicated that the pervasiveness of earnings management did not decline, but rather increased after the adoption of IFRS in France.

METHODOLOGY

Data for the study are gathered from secondary sources. The justification for the use of secondary source of data is inherent in the nature and measurement of the variables to be utilised in the study. Data is gathered from the annual reports and financial statements of 23 companies listed under the agriculture, conglomerate, construction and healthcare sectors of the Nigerian Stock Exchange for a period of 4 years; pre and post IFRS adoption. The hypotheses utilised in the study are given as follows:

Ho_1: There is no significant relationship between IFRS adoption and the value relevance of financial information.

Ho_2: There is no significant relationship between IFRS adoption and earnings quality in Nigeria.

Ho_3: There is no significant relationship between IFRS adoption and earnings management in Nigeria.

The study utilises three regression models to capture the changes in each of the variables over the given time spectrum. Model 1 is used to capture the proxy for value relevance, measured by market value of the firm. Model 2 is used to capture the proxy for earnings quality; measured by accrual quality, while model 3 is used to capture the proxy for earnings management; represented by discretionary accruals. The models are given as follows:

Model 1: (Pre-IFRS) $MV = \beta_0 + \beta_1 PAT + \beta_2 BVE + \beta_3 NOSH + U_t$. . (a)

(Post-IFRS) $MV = \beta_0 + \beta_1 PAT + \beta_2 BVE + \beta_3 NOSH + U_t$. . (b)

Model 2: (Pre-IFRS) $ACCR = \beta_0 + \beta_1 OCF + \beta_2 \delta REV + \beta_3 PPE + U_t$. . (a)

(Post-IFRS) $ACCR = \beta_0 + \beta_1 OCF + \beta_2 \delta REV + \beta_3 PPE + U_t$. . (b)

Model 3: (Pre-IFRS) $DACC = \beta_0 + \beta_1 REV + \beta_2 PPE + \beta_3 WC + \beta_4 EBIT + U_t$. (a)

(Post-IFRS) $DACC = \beta_0 + \beta_1 REV + \beta_2 PPE + \beta_3 WC + \beta_4 EBIT + U_t$. (b)

Where

MV = Market Value
PAT = Profit after Tax for Continuing Operations
BVE = Book Value of Equity
NOSH = Number of Ordinary Shares
ACCR = Total Accruals
OCF = Operating Cash Flow
δREV = Change in Revenue
PPE = Property, Plant and Equipment
DACC = Discretionary Accruals
WC = Working Capital
EBIT = Profit before Interest and Tax

The models are adapted from the work of He *et al.* (2009), but are modified to suit the objectives of the study. The data is analysed using the ordinary least square (OLS) regression methodology. Each model is analysed for each of the years covered by the study and for each of the variables under consideration.

The adjusted R^2 obtained from the regression results is used to determine the trend of the financial reporting proxies. Increases in the adjusted R^2 figure along the years indicate improvements in value relevance of the financial data, improvements in earnings quality, and increases in earnings management practices, while reduction in the R^2 figure entail decreases in value relevance, earnings quality and earnings management practices.

RESULTS AND DISCUSSIONS

Table 1 shows the descriptive statistics of the variables used in the analysis. The table shows that between the years under consideration, the average stock price of all the companies utilised in the study was about 15.75. The measure of earnings quality and earnings management however maintained an overall negative average with total accruals having a mean of -224,853, while discretionary accruals maintained a mean of -0.002. All the independent variables utilised (PAT, BVE, NOSH, EBIT, OCF, REV, PPE, and WC) however, maintained positive averages.

Discretionary accruals (DACC) displayed the lowest degree of volatility with standard deviation of 0.026, while revenue (REV) exhibited the highest degree of volatility, with a standard deviation of 36,286,722. Most of the variables were skewed to the right, with the exception of total accruals (ACCR), discretionary accruals (DACC) and earnings before interest and tax (EBIT), which were negatively skewed. Also, all the variables used in the study are normally distributed as observed from the Jarque-Bera statistics.

Table 1: Descriptive statistics

	Mean	*Median*	*Maximum*	*Minimum*	*Std. Dev.*	*Skewness*	*Jarque-Bera*	*Prob*	*Obs*
MV	15.74935	6.01	100	0.5	23.98078	2.263048	158.84	0	92
ACCR	-224,853	-37,953	13,597,801	-20,003,858	4,043,514	-1.593211	391.04	0	92
DACC	-0.00209	-0.000225	0.07499	-0.14102	0.02598	-2.378094	666.08	0	92
PAT	896,631	196,489	7,772,055	-6,650,384	2,061,300	0.388506	51.16	0	92
BVE	6,299,776	2,819,520	40,317,160	-11,244,174	9,422,112	1.613488	67.98	0	92
NOSH	2.43E+09	9.57E+08	3.87E+10	4,000,000	6.03E+09	4.347291	1,693.28	0	92
EBIT	1160915	242260.5	11544980	-15,519,000	3,284,107	-0.400159	248.70	0	92
OCF	1385767	353830.5	31548838	-9,099,761	4,586,824	4.010118	2,111.36	0	92
REV	13588897	4694410	1.97E+08	156,049	36,286,722	4.315102	1,431.53	0	92
PPE	5235048	2183443	66542850	0	11,955,768	4.173574	1,319.46	0	92
WC	2670442	729582	75029263	-42,464,131	11,414,335	2.861443	1,600.06	0	92

The hypotheses for the study are tested using the regression analysis. The models are constructed such that the dependent variables capture the value relevance, earnings quality and earnings management of the accounting information contained in the financial statements, while the independent variables jointly combine to explain the degree of variations in financial reporting quality for the respective period. The variations in the reporting quality are captured by fluctuations in the explanatory power of the independent variables; captured by the $\boldsymbol{R^2}$ statistics.

Hypothesis one is analysed using Table 2 (pre-IFRS) and table 3 (post-IFRS). The adjusted $\boldsymbol{R^2}$ statistics of table 2 indicates that about 5% of the total systematic variations in the value relevance of the accounting information is explained by a combination of the independent variables. This statistics increases to about 17% post-IFRS period measured by the same variables as outlined in Table 3. This means that adoption of IFRS in Nigeria has led to significant improvements in the value relevance of financial information; thereby enhancing the quality of financial reporting.

Hypothesis two is analysed using table 4 (pre-IFRS) and table 5 (post-IFRS). The adjusted $\boldsymbol{R^2}$ statistics increased from about 28% before the adoption of IFRS (table 4) to about 79% after the adoption of IFRS (table 5). This reveals that the quality of reported earnings improves post-IFRS adoption; hence, an improvement in the quality of financial reporting after the adoption of IFRS.

Hypothesis three is analysed using table 6 (pre-IFRS) and table 7 (post-IFRS). The adjusted $\boldsymbol{R^2}$ statistics of table 6 indicates that about 76% of the total systematic variations in the existence of earnings management practices (represented by the extent of discretionary accruals), is captured by the totality of the independent variables. This statistics decreases to about 59%

Table 2: Value Relevance pre-IFRS

Dependent Variable: MV
Method: Panel Least Squares
Sample: 2010-2011

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	13.01884	3.819480	3.408538	0.0015
PAT	3.31E-06	2.35E-06	1.408767	0.1663
BE	-7.42E-08	6.18E-07	-0.120044	0.9050
NOSH	-7.77E-10	6.18E-10	-1.257619	0.2155

R-squared	0.109574	Mean dependent var	13.37826
Adjusted R-squared	0.045972	S.D. dependent var	21.41639
S.E. of regression	20.91831	Akaike info criterion	9.002068
Sum squared resid	18378.19	Schwarz criterion	9.161081
Log likelihood	-203.0476	Hannan-Quinn criter.	9.061635
F-statistic	1.722815	Durbin-Watson stat	1.512483
Prob(F-statistic)	0.017690		

Table 3: Value relevance post-IFRS

Dependent Variable: MV
Method: Panel Least Squares
Sample: 2012-2013

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	13.98842	4.344086	3.220106	0.0025
PAT	4.25E-06	2.47E-06	1.722705	0.0923
BE	2.67E-07	5.48E-07	0.487138	0.6287
NOSH	-9.00E-10	6.24E-10	-1.443626	0.1563
R-squared	0.224717	Mean dependent var		18.12043
Adjusted R-squared	0.169340	S.D. dependent var		26.32071
S.E. of regression	23.98884	Akaike info criterion		9.275996
Sum squared resid	24169.51	Schwarz criterion		9.435008
Log likelihood	-209.3479	Hannan-Quinn criter.		9.335563
F-statistic	4.057922	Durbin-Watson stat		1.358810
Prob(F-statistic)	0.012779			

Table 4: Earnings quality pre-IFRS

Dependent Variable: ACCR
Method: Panel Least Squares
Sample: 2012-2013

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	213162.4	530945.2	0.401477	0.6901
OCF	-0.694267	0.258028	-2.690660	0.0102
REV	0.040092	0.078256	0.512322	0.6111
PPE	-0.057239	0.231102	-0.247677	0.8056
R-squared	0.331405	Mean dependent var		-382023.1
Adjusted R-squared	0.283648	S.D. dependent var		3795879.
S.E. of regression	3212740.	Akaike info criterion		32.88609
Sum squared resid	4.34E+14	Schwarz criterion		33.04510
Log likelihood	-752.3800	Hannan-Quinn criter.		32.94565
F-statistic	6.939434	Durbin-Watson stat		1.410651
Prob(F-statistic)	0.000674			

Table 5: Earnings quality post-IFRS

Dependent Variable: ACCR
Method: Panel Least Squares
Sample: 2012-2013

Variable	Coefficient	Std. Error	t-Statistic	Prob.
OCF	-1.138076	0.110692	-10.28151	0.0000
REV	0.053771	0.039137	1.373913	0.1766
PPE	0.074415	0.102604	0.725264	0.4722
R-squared	0.794172	Mean dependent var		-67682.02
Adjusted R-squared	0.784598	S.D. dependent var		4313251.
S.E. of regression	2001840.	Akaike info criterion		31.92002
Sum squared resid	1.72E+14	Schwarz criterion		32.03928
Log likelihood	-731.1606	Hannan-Quinn criter.		31.96470
Durbin-Watson stat	1.516829			

Table 6: Earnings management pre-IFRS

Dependent Variable: DACC
Method: Panel Least Squares
Sample: 2010-2011

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.000657	0.002409	0.272637	0.7865
REV	-3.34E-10	2.91E-10	-1.145261	0.2587
PPE	-8.72E-10	8.60E-10	-1.013550	0.3167
WC	-6.02E-11	2.97E-10	-0.202740	0.8403
EBIT	5.74E-09	6.80E-10	8.452245	0.0000
R-squared	0.778431	Mean dependent var		-0.002947
Adjusted R-squared	0.756815	S.D. dependent var		0.024355
S.E. of regression	0.012011	Akaike info criterion		-5.903741
Sum squared resid	0.005914	Schwarz criterion		-5.704975
Log likelihood	140.7860	Hannan-Quinn criter.		-5.829282
F-statistic	36.01103	Durbin-Watson stat		2.243232
Prob(F-statistic)	0.000000			

Table 7: Earnings management post-IFRS

Dependent Variable: DACC
Method: Panel Least Squares
Sample: 2012-2013

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.003701	0.003538	-1.045980	0.3017
REV	-1.46E-09	3.05E-10	-4.791581	0.0000
PPE	2.13E-09	9.37E-10	2.270467	0.0285
WC	-1.14E-10	4.27E-10	-0.266787	0.7910
EBIT	7.14E-09	2.43E-09	2.942414	0.0053

R-squared	0.629312	Mean dependent var	-0.001234
Adjusted R-squared	0.593148	S.D. dependent var	0.027754
S.E. of regression	0.017703	Akaike info criterion	-5.127885
Sum squared resid	0.012849	Schwarz criterion	-4.929120
Log likelihood	122.9414	Hannan-Quinn criter.	-5.053427
F-statistic	17.40131	Durbin-Watson stat	2.082163
Prob(F-statistic)	0.000000		

Table 8: Summary of hypothesis test

Measure of FRQ	***R^2* pre-IFRS**	***R^2* post-IFRS**	**Decision Criteria**	**Impact on Financial Reporting Quality (FRQ)**
Value Relevance	5%	17%	Reject $\mathbf{Ho_1}$	Improves FRQ
Earnings Quality	28%	79%	Reject $\mathbf{Ho_2}$	Improves FRQ
Earnings Management	76%	59%	Reject $\mathbf{Ho_3}$	Improves FRQ

post-IFRS (table 7) period measured by the same variables. This entails that the adoption of IFRS in Nigeria has led to a decline in the execution of earnings management practices by corporations, thereby enhancing the quality of financial reporting.

Hence for all proxies utilised, an increase in financial reporting quality was observed for the relevant years. A summary of the results of each hypothesis is outlined in table 8.

The study reveals that the adoption of IFRS in Nigeria led to improvements in the value relevance of accounting information contained in the financial statements. This finding supports the tenet of IFRS being viewed as a financial reporting system supported by strong governance, sound regulatory framework and high quality standards that improves the overall quality of financial reporting. The result of improvements of financial reporting quality in terms of value relevance was in consonance with the work of Palea (2013); which concluded on the improvement of financial reporting quality after the adoption of IFRS based on a meta-analysis. The finding is also in agreement with the works of Muller (2014), Kargin (2013), Lin *et al.* (2012), and Paglietti (2009). The result was however in contrast with the findings of Garanina and Kormiltseva (2013) which found no evidence of increased value relevance of accounting data to external users of financial information.

The results of the study also confirmed that there is a statistically significant increase in the quality of earnings after the adoption of IFRS in Nigeria. This was represented by a massive increase in the adjusted $\boldsymbol{R^2}$ figure from 28% before the adoption of IFRS to 79% after the adoption of IFRS. The finding of the study was in agreement with the works of Ismail *et al.* (2013), Sellami and Fakhfakh (2013), Assidi and Omri (2012) and Sun *et al.* (2011). The findings of Ames (2013), Nullah (2013) and Hoque *et al.* (2012) however stipulated that IFRS adoption does not lead to increased earnings quality.

The study also revealed that earnings management significantly reduced in the post-IFRS period. Studies that portrayed similar results include those of Dimitropoulos *et al.* (2013), Karampinis and Hevas (2013), Marra *et al.* (2011), and Liu *et al.* (2011). Some studies also had contrary findings to that of the study. Ahmed *et al.* (2013) in their meta-analysis found that discretionary accruals did not reduce post-IFRS adoption, while Doukakis (2013) found that mandatory IFRS adoption had no significant impact on either real or accrual based earnings management practices.

CONCLUSION

IFRS is driving the revolutionary world of accounting with over 120 countries either requiring or permitting its use. Organisations must fully understand benefits and challenges of the adoption in order to enhance their implementation and utilisation of the standards. Hence, professionals must be prepared to 'learn, unlearn and relearn' in order to minimise any negative impact, while maximising the benefits associated with IFRS adoption in the short, medium and long term (Omoye and Aderin, 2014).

The need to ascertain the effectiveness of the adoption of IFRS in enhancing the quality of financial reporting forms the crux of this research. Through an understanding of this, the study therefore sets out to analyse the overall effectiveness of the adoption of these standards in enhancing value relevance, earnings quality, and reducing the extent of earnings management practices.

The results of the study reveal that the adoption of IFRS has overall benefits in terms of improving the quality of reported financial information. It can also be concluded that the adoption of IFRS will have significant prospects as well as challenges on the activities of stakeholders. Specifically the benefits that would be derived from the adoption of IFRS as gleaned from our study indicate that IFRS on the overall would enhance financial reporting quality while reducing the probability of earnings management practices. This shows that IFRS adoption could be beneficial in the long run to the Nigerian financial landscape.

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