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Prospects and Challenges of Financial Reporting in Nigeria

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Abstract: *The study examines the effectiveness of International Financial Reporting Standards (IFRS) on financial reporting in Nigeria. The study is based on secondary data and descriptive in nature. Thereafter, content analysis method was used to highlight legal, environmental, and cultural challenges peculiar to Nigeria. The findings show that standards used in developed nations are also being applied to corporate entities in Nigeria to give adequate information to all stakeholders in financial reporting. Nevertheless, the neglect of corporate governance practices had led to significant losses to nearly all the stakeholders. Therefore, the study recommends among other things that additional standards should be included in accounting reports like translating accounting reports into the three officially recognized indigenous languages in Nigeria and addressing information overload in the accounting report.*

Key words: *Accounting Scandals, Adoption, Board of Directors, Comparability, Harmonization, Standards*

INTRODUCTION

Recording of transactions and daily activities vary from one culture to the other. In some cultures, financial transaction activities were recorded by markings on the walls by chalk or wax or on the trees by spikes or hooks. Cam woods and chalks were also used by the traditionalist in recording counts or marks in respect of initiations carried out. Transactions were also recorded on wax and tablets. Later, cowries were introduced to financial transactions when the trade by barter was jettisoned for money. The real accounting in financial transaction between merchants and traders were not as easy as it is today because the entity transactions was singular without taking into consideration the dual entity or double entry transaction was propounded by Lucas Pacioli in his treatise on double entry in commercial transaction in 1494. His treatise, "*Suma Arithmetica Geomatria Proportioni et Proportionalita*" meaning "Everything about Arithmetic, Geometry and Proportion", dealt on double entry system of bookkeeping which were based on three records of memorandum, the journal and the ledger. A section of the book entitled *De Computis et Scripturis* contained discussions on double entry book-keeping. Pacioli who was a professor of mathematics was learnt to have spent some time as an apprentice to a Florentine merchant. This exposure might probably had contributed to his background in writing Summa. This was useful for the merchants in based in Milan, Florence, Naples and Venice (citation) this made records involving business transactions with partners to be recorded in dual form. The basic principle was that for every transaction, there is a giver and a receiver, which resulted to the axiom that for every debit entry, there is a credit entry. This early rudiment of accounting through double entry system of bookkeeping allowed profits to be determined and distributed in ventures with business partners. The dual main soul of accounting then became debit and credit as demand and supply was that of economics.

The above accounting system did not adequately address the stewardship accounting function of reporting what had happened financially during the past period. This allowed dividend to be paid before the all the financial implications were considered. The periodicity concept was lacking. Standardized period of time when financial statements should be prepared was not in existence. A venture type of accounting was the order of the day and the creditworthiness of business partners was not available to one another. The overall profitability or otherwise of the business was impossible to be determined by this accounting convention.

In order to determine the profit or otherwise of the business, Simeon Stevin advocated the yearly preparation of profit and loss account in 1605 so as to allow businessmen know how profitably the business performed in the last one year. With this introduction of preparation of profit and loss account, the management and other stakeholders were able to know the performances of the business venture in the past twelve months. Later by 1655 the idea of drawing up a balance sheet at the end of a particular period was propounded by Jacques Savary. This would allow the owners to know the amount of assets and liabilities at a point in time. This was further made popular by the code of Commerce in France that recommended that a balance sheet should be prepared at least once in two years.

As a result of industrial revolution, business activities frog jumped from where it was to an unimaginable height. Business boomed everywhere, demand and supply of raw materials and finished goods increased. Joint stock companies emerged and the owners of businesses were eventually being separated from the management. This then necessitated demand for a more reliable accounting system to cope with the volume of business and reporting requirements of the period to satisfy the need of various accounting users. Thus, began the divorce of management from ownership as it was evident that accounting information were needed by various users of financial statements like shareholders, governments, revenue officers, would-be investors, creditors, suppliers etc.

The Society of Accountants in Scotland was granted a royal charter in 1854 and this was followed with the formation of the Institute of Chartered Accountants of England and Wales in 1880. Across the Atlantic in the United States of America, the Association of Public Accountants was launched in 1887. The code of ethics of and conduct of these professional accountancy bodies had their positive impact on the development of accounting most especially financial statements of business entities.

The accounts kept by many businesses merely consisted of cash and inventory movements without taking into considerations the accrual and prepayments conventions. This often resulted to depletion of capital as dividends were wrongly paid before profits were finally determined. Provisions for bad and doubtful debts were not provided for and fixed assets were bought and used up without providing for depreciation.

The industrial growth and the concept that the world is a global village coupled with the contributions by various professional accountancy bodies made it necessary that financial statements should be easily understandable to the users of accounting information. This now compelled each nation to individually conceptualize accounting information that are relevant to the local standards and also to be involved in international accounting standards that will cut across national borderlines.

In 1982, the Nigerian Accounting Standard Board (NASB) established to provide the standard required in preparation of financial statements through issuance of standards (Statement of Accounting Standards) for the local needs. In 1989, the International Accounting Standard Committee (IASC) was inaugurated and it was saddled with the responsibility of producing a conceptual framework for preparation and presentation of an internationally acceptable financial reporting and presentation of standard named as International Accounting Standard (IAS). A reorganization took place in 2001 which changed the working policy of International Accounting Standard Committee (IASC) that led to its name being changed to International Accounting Standard Board (IASB). Some of the International Accounting Standards (IAS) were adopted and modified to produce the new accounting framework and concepts known as International Financial Reporting Standards (IFRS) for preparation and presentation of financial reports globally. This was adopted by many countries in 2005. Japan and China adopted a roadmap in 2009.

In order to comply with global changes to IFRS, the Nigerian Security and Exchange Commission (SEC) issued directives to all business entities operating in Nigeria. They are directed to adopt IFRS for the preparation and presentation of their financial statements effective from January 1st 2012. The small scale and medium enterprises had their effective date as January 1st 2013.

Meanwhile, Nigeria had signed into law an Act establishing Financial Reporting Council of Nigeria (FRCN) in 2011 after the repeal of Nigerian Accounting Standard Board (NASB). Financial Reporting Council of Nigeria (Act 22 of 2003) is charged with the responsibility for developing and publishing accounting and financial reporting standards to be observed in the preparation of financial statement of public entities in Nigeria. The adoption of IFRS in Nigeria had made financial reports to be comparable when harmonizations of standards are taken into consideration.

The International Public Sector Accounting Standards (IPSAS) was adopted by the public sector with effective date of January 1st 2015.

In order to emphasize the principles and concepts of financial reporting, the code of corporate governance made it mandatory that directors of public companies should properly be accountable to the shareholders by rendering not only financial reports that are of high standard but also narrative reporting that are self explanatory to the users of financial statements. External audit of the financial statements will give assurance to the credibility of the financial reporting. With these, financial statements will be more useful to all the stakeholders. However, of recent are the losses of confidence in corporate financial statements being eroded through manipulation or misappropriations being perpetrated by some of the stakeholders most especially the management with the support of the auditors of the companies. Because of these infractions, all safeguards formulated and developed by the professional accountancy bodies, the national regulatory financial systems and the international financial bodies to fulfill the objectives of financial reports are easily thwarted (Wilson, Iheanyi, Okoroafo & Onyilo, 2016).

The boards of directors, in collusion with employees, are sometimes involved in accounting scandals due to inadequate corporate governance mechanism.

Moreover, these infractions had no respect for boundaries, as national and international corporations are victims of this malaise. Objectives of financial statement are no longer fulfilling their purposes as they should and this is a challenge to academics and professional accountants.

The above now raises the question of developing theories that would be more purposeful to the accounting reports that that will be globally effective in all its ramifications as the present concepts and framework are not addressing the shortcomings emanating from different countries. What are the prospects and challenges of International Financial Reporting Standards (IFRS) to Corporate Governance in Nigeria? Pin pointedly, what are the limitations of the present accounting concepts and regulatory framework that fail to meet the expectations of the users of accounting reports?

In order to find solution to this, the focus of this paper will be the effectiveness of the financial statements to the users of accounting reports. Hereafter, the paper is then divided into four sections. Conceptual framework is in chapter two; research methodology will be in chapter three; chapter four is on findings and discussion. Summary, conclusion, and recommendation will be in chapter five.

Conceptual Framework and Literature Review

Conceptual Framework

- **Financial statement**

The International Accounting Standard Committee (IASC) metamorphosed into International Accounting Standard Board (IASB) in 2001. The board's framework pinpointed issues pertaining to the preparation and presentation of financial statements. The objective of financial statement, according to IASB is to provide information about the financial position, financial performance, and changes in financial status of an entity, which will be useful to a wide range of users in making informed economic decisions. In preparing a high quality financial reporting, private sectors' growth is enhanced and the economy is strengthened with a low risk of financial market crises. Foreign investors can easily evaluate corporate prospects thereby making informed economic decisions. Financial statement is expected to be easily understandable by all the users an d it must also be relevant to the business concerned. So also, the attributes of relevance, comparability, reliability, and uniformity are of paramount importance a financial statement should possess before justifying its usefulness to the stakeholders.

- **Disclosure of information in the financial statement**

In compliance with Companies and Allied Matters Act Cap C 20 Laws of the Federation of Nigeria, 2004 (as amended) the following information are to be disclosed in the financial statement.

- ✓ Statement of accounting policies
- ✓ Profit and loss account
- ✓ The balance sheet
- ✓ Value Added statement
- ✓ Five Year financial summary
- ✓ Notes to the account
- ✓ Auditors’ report
- ✓ Directors’ report
- ✓ Group financial reports in case of group of companies

However, based on the newly adopted International Financial Reporting Standards operating in Nigeria, the following are the information that are to be disclosed to enhance comparability and transparency of the information disclosed.

- ✓ Statement of financial position
- ✓ Statement of comprehensive income
- ✓ Statement of changes in equity
- ✓ Cash flow statements
- ✓ Notes to the accounts

- **Stakeholders of financial reports**

The stakeholders of any financial statements are ordinarily parties that have interest in that document. They may be internal and external. Primarily, the stakeholders comprise investors and potential investors who are concerned with the security of their investments and the profits that they can earn. The security or otherwise of their investments will be revealed through the solvency of the company as stated by the assets and liabilities in the financial position of the firm at a particular point in time. Past performances can determine future profits through income statement. Lenders of funds are interested in the types of securities available and if they will be paid interests on the facilities. Suppliers need to know if goods and services rendered are to be paid for, and new suppliers require assurance about the financial health of the firm before supplying goods. Customers, especially those dependent on the company, will be interested to know if the firm is able to supply or produce goods and services into the future. Trade union representatives and employees are interested in the financial statements to know if the employers can offer secure employment and possible pat rises. The disclosure of salaries and benefits of senior managers may be of interest to them. Also useful is the divisional profitability of the business if threatened with closure. In order to plan for financial and industrial policies, government agencies are interested in the performance of companies through the financial statements. Tax authorities use the financial statements as basis for assessing companies for tax payable. Finally, the effect of the company on the economy, local environment, and local community will be of interest to the public. Corporate social responsibility programmes undertaken by the companies may be of special interest to some members of the public.

Literature review

Whenever revenues are matched with expenses, the resultant effect is the generation of income. Revenue itself is a flow of fund, which has resulted from the trading or business activities of a particular enterprise during a particular period, which is normally measured in twelve months. When revenues are more than expenses, there is gain, which is also called profit. When reverse is the case, there is loss. In order to be of any use to information users, income must be measured periodically (Eldon, 1982; Oseni, 2013). This leads to periodicity concept that stipulates that income should be measured once in a year. The measurement is also guided by accrual and prepayment concepts. The accrual concept makes clear distinction between cash received for goods and services and cash to be received later for the same goods and services. Therefore, to follow accrual concepts in totality, all costs (expenses) and revenue are accounted for whether paid for or not during the period covered by the financial report. Closely related to this is the matching concept that expects the financial statements to match the incurred costs in one year with the revenue of that year. All expenses incurred, but not meant for that particular period (prepayment) are to be excluded from the total costs. Unrealized profits should not be included with the revenue of that period.

The concept of capital and income are closely related. A stock of wealth existing at a given period of time is called capital whereas a flow of benefit from wealth of a given period of time is income. The income is derived from capital. One can say income depends to some extent on the size of the capital. Accounting income is a surplus derived from a business activity and it is measured by the use of matching concept when cost is set against revenue for a given period of time. Accountants measure income and try to ensure that the measurement is accurate and near to the truth as possible, therefore the accounting income is an ex post measurement. However, to the economist, income is defined as maximum amount an individual can earn during a period of time, which makes him to be as well at the end of the period as the beginning of the period. it then follows therefore that income is the amount the capital or net worth has increased during the given period and as to what has been withdrawn at the end of the period less new capital at the end of the period.

The objectives of income measurement are not farfetched from the concepts of the IFRS. Income is used as a basis for measuring efficiency. It shows how much the asset has generated. It also measures the company sources of revenue; it acts as a guide to future investment; it is an indicator of managerial effectiveness; it provides a basis for tax computation; it acts as a guide to the determination of firm's credit worthiness and provides a basis for dividend policy (Lee, 1974)

To the economist, capital means those assets that are used in production of goods and services. The capital of the firm is represented by the stock of assets and its investment is made when the firms' stock of capital is increased. Capital includes physical assets in form of buildings, plants, and machinery as well as intangible assets. So also human resources and technology. In addition, capital is considered as present value of future savings derived from an asset of enterprise as a whole so that capital and income are linked together. Economists may prefer broader definition of capital employed and might suggest some assets as human resources that are omitted by accountants in their definition because they cannot be quantified and recorded in the books.

To the accountant, Capital is the amount invested in an enterprise by their legal owners. Accountants measure capital with reference to tangible assets whose existence, ownership, and cost can be verified. As far as the accountant is concerned, a person's capital is increased by the amount of his periodic which he has not consumed.

Many concepts have been developed to ensure that financial reporting are made in such a way that the value of capital is not necessarily reduced or at least the value capital is maintained.

One of such concepts is the capital maintenance concept. The capital concept argues that since the objective of going into business is to increase the value of one's assets (capital) through maximization of profits/benefits, then profit should be distributed when profit is available and should not be paid out of capital.

Value is a useful concept in financial reporting which has its effect on the capital of an enterprise. The value of an asset is the present value of the future income stream expected to be derived from the assets.

The price of the asset is the value set on it in market place by the interaction of the demand and supply. The general belief is that when an asset is very expensive, it has a high value and when the price of an asset is low, the value of such asset is not high. As far as income is concerned, an asset that generates income must have a high value.

An asset will have different value according to the purpose, which it is made. Individual with different of the potentialities of an asset to produce income will value it differently. This shows clearly that the capital, value and income are strongly related. The incomes generated by an asset determine the value of that asset and such value determines what should be paid for the asset as income.

The primary objective of financial reporting is to enable investors and other users to be informed of investment decisions (Adetoso and Oladejo, 2013). Two reasons may be given for the interest of investors for the worth of their businesses. They are concerned with maintaining the cost of their capital and also concerned with maintaining and increasing their income, which is derived from the capital. Therefore, financial reporting concerns itself with capital and income. It is on this basis that financial reporting involves capital, income and value.

The accounting cycle consists of the following steps:

- ✓ Documentary evidence: It is the basis of recording a transaction e.g., a purchase invoice for recording purchases.
- ✓ Journalizing transactions: It is the recording procedure under double entry book-keeping.
- ✓ Posting to the ledger: It is the process of transferring transactions into various .accounts. An account is the basic unit of accounting that classifies diverse economic events into a homogeneous group.
- ✓ Balancing of accounts: Accounting is essentially aggregative in nature. The classification of transactions into homogeneous groups, called. accounts involve offsetting the positive flow against the negative flow of benefits. The remainder is called the balance of the accounts.
- ✓ Preparation of trial balance: A trial balance is the list of the balances of accounts arranged according to debits and credits such that the aggregate of the debit balances equals to the aggregate of credit balances. This is an apparent proof of the arithmetical accuracy of the balances of the accounts.
- ✓ Adjusting entries: Adjusting entries are the post trial balance operations which involve allocation of various items of revenues and expenses to the appropriate time period or operations for proper matching, e.g., depreciation adjustment, stock adjustment, etc.
- ✓ Preparation of final accounts: The last stage in the accounting cycle is the preparation of final accounts. This involves two steps-the first step is the closing of the temporary accounts (*i.e.,* revenues and expenses) which are not be carried forward to the next accounting period. The accounting stage for closing of the accounts is called income statement. The second step involves preparation of statement of financial position with the remaining balances of accounts that are not to be closed during the year to the income statement.

Accounting, on the one hand, is a practical art attempting to record, classify, and summarize certain facts and events relating to business. On the other hand, it can be viewed as a theory of financial communication founded on assumptions and containing logically derived and internally consistent conclusions. Like the most other fields of knowledge, accounting is also oriented to certain concepts, postulates, conventions, and assumptions. These concepts, postulates, convention and assumptions which provide the operational content of the subject or a frame of reference to achieve the goal of accounting is collectively known as accounting bases. Accounting bases provide an orderly and consistent framework for periodic reporting of financial transactions of business, which by their very nature are both complex and diverse.

In financial reporting, one of the most important aspects is income. To the stakeholders, income is the most important reason of participating in the business activities of the organization. The measurement of income occupies a central position in accounting. Income measurement is probably the most important objective and function of accounting, accounting concepts, principles and procedures used by a business enterprise. Income represent wealth increase and business success; the higher the income, the greater will be the success of a business enterprise. The following are some of the major areas where income information is practically useful:

Research Methodology

Secondary data were used for this study. Qualitative research approach and retrospective literature analysis which were mainly secondary sources were used in order to highlight legal, environmental, and cultural challenges of financial reporting based on IFRS peculiar to Nigeria. Relevant materials such as textbooks, Journals, Newspaper and other official documents that were relevant to the adoption of IFRS in Nigeria were also used.

Findings and Discussion

Financial reporting all over the world are prepared in languages understood by the stakeholders. Legal and cultural matters are translated to Scottish and Welsh languages from English languages in the United Kingdom. Even, papers in Law and Taxation in professional accountancy examinations often have local papers in these languages. However, this privilege is not extended or practiced in other lands colonized by the British. The option of having financial reporting in local languages will strengthen the corporate governance and dismantle cultural differences. Countries in Africa still use English language as its official language in financial reporting without any option for local language. The IFRS, which was adopted in Nigeria, has no provisions for local language translation which is a cultural element inherent in the standards.

Summary, Conclusions, and Recommendations

The main focus of this paper rests on prospects and challenges of International Financial Reporting Standards (IFRS) to corporate governance in Nigeria. The history of accounting worldwide including that of Nigeria was discussed. The contributions of various individuals, corporate bodies, and professional accountancy bodies towards the development of accounting from the earliest periods to the time the International Financial Reporting Standards was promoted and accepted worldwide. The local development of accounting was also discussed.

The financial reporting in other lands take into consideration the local attributes like the local languages into consideration. This paper recommends that local languages should be introduced into financial reporting as it is been done in advanced countries. Locally, sports commentaries are now being reported in local languages on foreign sports and the enthusiasms and contribution with followership are encouraging. The paper then concludes that local content like local languages should be introduced into financial reporting in Nigeria.

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