ETHICAL PRINCIPLES AND RELEVANCE OF FINANCIAL REPORTS OF QUOTED COMPANIES IN NIGERIA

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ABSTRACT: *Financial reports are meant to present relevant accounting information among other qualities required of them. The relevance of financial report is necessary in decision making; investors, lenders and other creditors place reliance on financial reports that reflect predictive and confirmatory financial information. However, some financial information have been known to be distorted or falsified; resulting in irrelevant and misleading reports that are not suitable for decision making. Using survey research design based on a population of 4893 accountants and auditors of 169 quoted companies and four regulatory bodies in Nigeria, the study investigated the relationship between ethical principles and relevance of financial reports. Four hundred copies of the research instrument with a reliability test coefficient of 0.830 using the Cronbach's alpha statistics were distributed with a 92.5% return rate. Data analysis employed the use of descriptive and inferential statistics. The results indicate that ethical principles influence the relevance of financial reports significantly (* $F(4, 366) = 36.721$, *Adj.* $R^2 = 0.279$, $p = 0.000$)*. The study recommends continuous ethical orientation for accountants, managers and auditors of Nigerian quoted companies.*

KEYWORDS: Ethics, Integrity, Financial Reports, Quoted companies, Relevance

INTRODUCTION

Understanding the connection between the principles of ethics and the quality of financial reports of quoted companies is necessary to appreciate the need for relevant and faithfully represented financial reports of quoted companies in Nigeria. This understanding is also necessary to appreciate the need for comparable, understandable, timely and verifiable financial reports of quoted companies. Providing financial information of high quality is necessary because of its influence on capital providers who rely on such information to arrive at investment decisions. Relevant financial information bears on the economic decisions for which it is deployed or used (Morton, 1974) and the quality of financial reports is positively related to investment efficiency (Chen, Hope, Li & Wang, 2011).

Part of the concern for high-quality financial reports is the development of International Financial Reporting Standards (IFRS) by the International Accounting Standards Board (IASB). The Board asserts that high-quality financial reporting would bring about transparency, accountability and efficiency to financial markets around the world (IASB, 2010). The quality of financial reports is a precondition for efficient and healthy capital markets, makes investment more attractive and assists investors to assess stewardship (how management has utilized entrusted resources).

From the perspective of the Conceptual Framework for financial reporting, it is the objective of general purpose financial reporting to provide financial information about an entity that is useful to stakeholders; particularly investors and lenders in arriving at decisions relating to providing financial resources to the entity (IASB, 2010). Implicit in this objective is the need to provide useful financial information. To be useful, financial information must possess certain qualities: relevance, faithful representation, comparability, understandability, timeliness and verifiability. Relevance and faithful representation are considered 'fundamental qualitative characteristics', while comparability, understandability, timeliness and verifiability are categorized as 'enhancing qualitative characteristics' required of financial information (IASB, 2010).

However, reported cases of accounting scandals have shown that accounting standards, legislations/regulations and auditing may not be enough to ensure quality financial reporting. Lois, Davey and Hooper (2008) observe that the accountants assist in financial management, preparation of financial statements and auditing yet accounting scandals and corporate collapses occurred. It is argued that these occurrences set a new low for the profession of accounting whenever they occur. Also, Jones (2012) observes a wave of accounting scandals through creative accounting and fraud across different countries in the late 1990s and early 2000s, particularly, the incidents involving WorldCom and Enron.

After WorldCom, Enron and other accounting scandals, a number of reactions occurred throughout the corporate and accounting worlds (Arya, Glover & Sunder, 2003). There was the call for more transparency and accountability as a way of resolving the ethical situations (Dando & Swift, 2003; Beu & Buckley, 2001; Dubrick, 2003). Stein and Salterio (2017) argue that the various accounting scandals are ethical dilemmas.

Nelson (2018) reports that the defunct Skye Bank's management has been involved in serial manipulation of financial statements including masking of details to deceive the regulators. Risk Assessment and Forensic Investigation report of the Nigeria Deposit Insurance Company shows that the erstwhile management of the bank engaged in banking malpractices and insider abuse, as well as false accounting, manipulation of financial statements (to declare false profits), unlawful loans and non-disclosure of directors' interests. The Central Bank of Nigeria revoked the operating license of Skye Bank Plc. on 22 September, 2018 and established Polaris Bank to assume the assets and liabilities of the defunct bank.

Print ISSN: 2053-4086(Print), Online ISSN: 2053-4094(Online)

Objective/Hypothesis of the study

The objective of the study is to examine the relationship between ethical principles (integrity, objectivity, diligence and professional competence) and financial reporting quality via Relevance. Relevance is a fundamental qualitative characteristic required of financial reports which makes them economic decision-useful. Thus, the study evaluated the relevance of ethical principles on the relevance of financial reports of quoted companies in Nigeria. Then the hypothesis formulated for the study is that ethical principles do not have significant effect on the relevance of financial reports of quoted companies in Nigeria.

Significance of the study

The relevance of accounting information is its influence on the judgments made by users, particularly the investors; how they conclude on investment choices. Therefore, reporting of relevant accounting information is ethically significant. The study of how ethics affect financial reporting quality in terms of relevance is necessary in assisting managements, accountants, auditors, regulatory bodies, policy makers and investors. And the finding of this study adds to the existing literature on ethics and its relationship with the relevance of financial of financial reports of Nigeria quoted companies. The study is to remind professional accountants who provide the technical expertise in financial reporting to remember and apply their profession's code of ethics.

REVIEW OF LITERATURE

Perspectives of Ethics

Ethics is determined from the evaluation of moral content of behaviour or an action. Thus, ethics is considered from three perspectives: consequentialist ethics, deontological ethics and virtue ethics (Kaptein & Wempe, 2002). Ethics comprises of the rules and principles of behaviour that guide our choice of what is right or what is wrong.

Consequentialist Ethics

In consequentialist ethics, the moral content of an action is determined by the effect/ result of the action. An action is described as good if its effect is desirable, if the effect is not desirable, it is a bad action. Because standards are employed to judge the consequences of actions, this aspect of consequentialist ethics is called teleological ethics. It is believed that actions are taken to achieve specific 'ends'. Ends are chosen as standards for judging the moral content of actions. The focus of teleological theory revolves around targeted ends, which can vary from individual to individual; referred to as ethical egoism. Ethical egoism falls short of generalisability, whereas utilitarianism holds that the common good of all should be the true end (Kaptein & Wempe, 2002)

According to Adam Smith; the pursuit of self-interest by individuals would indirectly address the welfare or common good of society. Utilitarianism is an ethical theory which holds that actions greatest benefit to society at the lowest cost. Jeremy Bentham (1748-1832) posits that all actions must be judged on the basis of "greatest pleasure for the greatest number". This implies that individuals or groups should act with the mind to maximize the common good of society as a whole and consequences need to be factored into actions.

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Deontological Ethics

Deontological, also called duty-based ethics, stipulates the duties that must be done and the rights that must be respected. Actions must correspond with certain principles; this is primarily what determines whether the action is morally right or wrong. An action is morally good if it honors a given obligation. Kaptein et al. (2002) posits that the foundation of deontological theory can be deduced from God's commandment (that duties are God-given), common sense or from a social contract. David Ross (1877-1971) argues that moral principles fall under prima facie duty that must always be honored unless there is a conflict with a more pressing obligation in a given situation. Kant (1724-1804) believes that moral rules are based on pure reasoning instead of conscience intuition or the consequences of action.

Virtue Ethics

While deontology is a theory of moral obligation that focuses on action as the basis of evaluation, virtue ethical theory focuses on the agent not the action. Virtue ethics considers the individuals directly from the perspective of motives, intentions and abilities. Kampe et al. (2002) describes virtues as a person's capacity to perform what is expected of him. Aristotle synthesized the ideas virtues. Thus, virtue is an ethical theory that formulates norms on the basis of human qualities or characteristics. Virtue ethics is also called "quality ethics". Plato considers virtue as the proper execution of given task or function. He recognizes wisdom, courage, moderation and justice as the principal virtues. For Aristotle, virtue is a state of character which enables a person to discharge his function well. Kant defines virtue as an internalized inclination to properly fulfil one's duties. MacIntyre defines virtues as obtainable human qualities.

However, virtues have five characteristics; Desirability, expressed in action, stable or durable character, Constance & subject to influence. Virtues are considered as predispositions to act in line with moral obligations

Qualities Required of Financial Information

Financial information, by character, can be expressed both in figures and words. They represent economic phenomena that have qualitative and quantitative values. In effect, these accounting figures must be faithfully represented (complete, neutral and error-free) and be decision-useful. This is because financial reports provide information regarding an entity's economic resources, effects of transactions that change these resources and claims against the entity. The conceptual framework for financial reporting identities fundamental qualitative characteristics as well as enhancing qualitative characteristics. The fundamental qualitative characteristics are faithful representation and relevance, while the enhancing qualitative characteristics are understandability, verifiability, comparability and timeliness (IASB, 2010). When financial reports possess these qualities, they become economically useful in terms of decision-making for both existing and would-be investors. Lenders, other creditors and the rest stakeholders also derive economic benefit from quality financial reports.

Relevance

The conceptual framework for financial reporting describes relevance of financial reports in terms of its confirmatory and predictive qualities (IASB, 2010). If financial information is to be of value, it must be capable of influencing or making a difference in the decisions made by users,

Print ISSN: 2053-4086(Print), Online ISSN: 2053-4094(Online)

particularly, investors. A financial report may possess either predictive or confirmatory value or both. The predictive value of a financial report is found in its ability to aid the processes used by users to predict future outcomes, while confirmatory value of a financial report is found in its ability to confirm previous evaluations. However, the predictive and confirmatory values of financial information are interwoven, while materiality is an aspect of relevance that is entity-specific. Materiality is a relative concept expressed in terms of the nature or magnitude of the items to which the information relates.

Power (2010) suggests that the relevance of financial information is in its ability to provide options in terms of decision making. This points to the capacity of financial reports in influencing its users towards arriving at economic decisions in terms of providing resources to a reporting entity. Potential and existing investors, lenders and other creditors expect to find financial reports that provide promising and forward-looking accounting information that suggests beneficial future cash inflows. Barth, Beaver, and Landsman (2001) explain that the extent or how well accounting amounts convey information that equity investors use is its relevance. An accounting amount is considered value relevant if it reflects a predicted association with market worth of equity. That is, the relevance of financial reports is measured in terms of its significant association with share prices.

Barth, et al. (2001) distinguish relevance from reliability. Relevance is expressed in the correlation between accounting amounts and equity values, while reliability is expressed in the correlation between accounting amounts and faithful representation (accounting amount representing what it purports to represent). Further distinction is also drawn between value-relevance and decision-relevance: Timeliness of information makes the difference. That is, an accounting information may be relevant in value but not relevant in decision making because of the timelines in information supply. Relevance of accounting information has significant relationship with fair value estimates. The study of bank loans by Barth et al. (1996) shows that fair values of bank loans are perceived by investors to reflect underlying values with more relevance and reliability than historical cost figures. Erin, Olojede and Ogundele (2017) note that the relevance of financial information is its power to effectively impact the decision of investors on investment issues. Financial information is relevant in determining the value of share prices and subsequently relevant in decision making in the capital market (Sutopo, Kot, Adiati & Ardila, 2018).

Faithful Representation

Financial reports are expressed in numbers and words do depict economic transactions and other events. Since useful financial report represent economic phenomena, it is expected that it should be a faithful representation of such phenomena. Thus, the faithful representation of financial report is found in its completeness, neutrality and freedom-from-error (IASB, 2010). A financial report is considered complete, if it reflects all the information it ought to reveal. These are financial information arising from transactions and other activities of an entity. Completeness of a financial report also extends to the narrative and clarification of significant facts about transactions and other events. Neutral depiction of financial report is shown in the objectivity and fairness in the preparation of financial information. A neutral financial information is devoid of bias nor any form of manipulation. Error-free depiction of financial report points to the absence of errors or omissions in the description of the economic phenomena.

Print ISSN: 2053-4086(Print), Online ISSN: 2053-4094(Online)

Enhancing Qualitative Characteristics

The enhancing qualitative characteristics, as the name suggests, are those qualities that improve the fundamental qualitative characteristics of financial reports. These factors enhance the 'relevance' and 'faithful representation' of financial reports. They are; comparability, understandability, timeliness and verifiability (IASB, 2010).

Comparability

Comparability is the quality that enables users to compare financial reports of an entity through time, and also compare financial reports of entities over time in order to identify trends in its financial performance and financial position (Cheung, Evans & Wright, 2010). It enables users to compare entity to entity in order assess their performances. It is necessary for users of accounting figures to relate financial reports with one another, to allow them make sound and informed decisions arising from financial information that has been prepared to enable comparisons within the same entity over time and between entities (Tootell, 1963; Dunn, 1975; Bell, 1982; Van der Tas 1992; Sharpe, 1998). When companies operate in a comparable manner, they make the same selections between alternative accounting methods. IASB (2010) states that comparability is an enhancing qualitative characteristic that helps users to understand and identify the similarities and differences that exist among items. Information is more valuable if it can be compared with information about the same entity and about other entities with similar information. However, comparability is not the same with consistency, nor with uniformity, although consistency relates to comparability.

Understandability

Understanding financial reports is required for knowledge that enables investors to make informed decisions. A financial report that is not understandable is not worth its content. IASB (2010) states that the process of classifying, characterizing and presenting financial information concisely and clearly makes it understandable.

Timeliness

Timeliness of financial information points to the need for timely delivery of accounting report as required by regulation or guideline. IASB (2010) states that making information available in time to makers of decisions to be capable of influencing their decisions means timeliness. Information is more useful and decision-relevant when it is new. When information is old, it becomes less useful. Johnson and Zhang (2018) opine that information technology enhances the speed of the production of financial reports. It is also required for the efficiency of auditing of the reports. In Nigeria for instance, Okougbo and Efobi (2014) observe that the fastest reporting company takes an average of 122 days, some take as much as 304 days. This is in contrast to the requirement of the Security and Exchange Commission's 90days. The study shows that size, leverage and performance are negatively correlated with the timeliness of corporate financial reporting while age is positively correlated with the timeliness of financial reporting.

Verifiability

Verifiability denotes that well-informed and independent observers could arrive at an agreement. This does not imply that the different well-informed and independent observers are in complete

Print ISSN: 2053-4086(Print), Online ISSN: 2053-4094(Online)

agreement (IASB, 2010). Verifiability is an assurance quality of financial reports that helps to assure the users that the accounting information is faithfully represented with respect to the economic phenomena it purports to represent. Verifiability helps to confirm, through the examination of report in a direct or indirect manner. Directly, there could be an investigation of the physical existence of assets or the verification of the carrying amount of inventory by checking the quantities and costs and recalculating the inventory as at a given date.

METHODOLOGY

The survey research design was adopted for the study; involving the collection of data through the administration of structured questionnaire on accountants and auditors of quoted companies in Nigeria, as well as accountants and auditors of quoted companies' regulatory agencies in Nigeria. The questionnaire was sectionalised to reflect demographic information, independent variables and dependent variables. Responses were rated using the five-point Likert scale. Internal consistency (reliability test) was carried out on the research instrument; using Cronbach Alpha reliability test, with the aid of Statistical Package for Social Sciences (SPSS). The result of the test shows coefficients range between 0.756 and 0.973 among the constructs. Given these results, it is concluded that the instrument is reliable and capable of producing consistent results.

Four hundred copies of the questionnaire were distributed to the respondents, three hundred and seventy were retrieved and analysed using associational and inferential statistics. The associational statistics tested the correlation between the variables, while the inferential statistics was meant to test the hypotheses and consequently draw conclusions.

FINDINGS

Table 1: Relevance and Ethical Principles

	Coefficient	(t-stat)	[p-value]
(Constant)	1.386	(15.191)	[0.000]
INT	0.026	(0.368)	[0.713]
OBJ	0.237	(2.906)	[0.004]
PC	0.235	(2.633)	[0.009]
DIL	0.076	(1.21)	[0.227]
Observation	370		
F-stat [*p*-value]	36.721		[0.000]
R^2	0.287		
Adj. R^2	0.279		

Source: Author's computation, underlying data from field survey, 2018.

From the result in table 4.1, Relevance (a financial reporting quality indicator) is considered as a dependent variable, while integrity, objectivity, professional competence and diligence (ethical principles) are considered as independent variables. Interpreting this result; the F-statistics values of 36.721 [p = 0.000] indicate that the ethical principle indicators are jointly statistically significant at 1% alpha level. Also, the Adj. R^2 value of 0.279 indicate that the independent variables jointly

Print ISSN: 2053-4086(Print), Online ISSN: 2053-4094(Online)

explain 27.9% the variations in Relevance. Relevant financial information bears on the economic decisions for which it is deployed or used (Morton, 1974) and the quality of financial reports is positively related to investment efficiency (Chen, Hope, Li & Wang, 2011). Financial reports have predictable relation with the prices of shares.

The relevance of financial information assist users, particularly investors, to arrive at informed economic decisions. Because relevant information is significant in making a difference in the decisions made by users; by assisting them in the evaluation of the effects of past and present transactions on future cash flows (this is referred to as the predictive value). Relevant information also assist users to confirm their earlier evaluations of financial information (this is referred to as the confirmatory value). Attempts at preventing unwholesome financial reporting practices and aiming at improving financial reporting quality has often been addressed from the technicalities of financial reporting; the ethicalities beg for attention. Preparers of financial reports do play games and manipulate accounting numbers; this is evident in accounting scandals and business failures recorded at different times across the globe. To this end, human factor comes to play; accountants and managers do influence the content of financial reports, while auditors do collude. It is necessary for accountants to collate financial information that are relevant to decision making, from sources that have financial decision significance.

Contribution to knowledge

The main thrust of this study is the examination of the impact of ethical principles on the relevance of financial reports of quoted companies in Nigeria. This study is one of the few that cut across all the sectors of the Nigerian economy by employing a bigger sample size of respondents relative to other studies. With this methodology, the study eliminates the limitation associated with previous studies. The study considered ethics from its various perspectives. Finding from the study has updated the literature on how ethics positively and significantly affect the production of relevant financial reports, especially from the Nigerian perspective. The study has affirmed the theory of ethics from the perspectives of consequentialism, deontology, virtues and integrity.

CONCLUSION AND RECOMMENDATION

The study concludes that the production of relevant financial information of quoted companies requires the application of the ethical principles of integrity, objectivity, diligence and professional competence. Relevance is a fundamental attribute necessary to add value to financial reports, therefore, ethical orientation and reorientation of accountants, auditors, managers and regulators is necessary to instil ethical values in them. It is suggested that the public sector can be studied in terms of how ethics affect the relevance of its financial reports. Companies that are not listed may also be studied.

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Print ISSN: 2053-4086(Print), Online ISSN: 2053-4094(Online)