# FAITHFUL REPRESENTATION OF ACCOUNTING INFORMATION AND FINANCIAL PERFORMANCE OF QUOTED BANKS IN NIGERIA

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**ABSTRACT:** *The study examined faithful representation of accounting information and financial performance of quoted banks in Nigeria using secondary data obtained from Nigeria stock exchange spanning from 2007 to 2016. Price to earnings ratio- PER and Earnings yield- ENY were selected as financial performance proxies while absolute discretionary accruals (ABSDA) was used as a measure of faithful representation of accounting information. ABSDA was subjected to Hausman test and also regressed against performance variable. Findings indicate that ABSDA is negatively correlated with PER but positively correlated with ENY. The study also confirmed a significant negative effect of ABSDA on PER and ENY implying that the more intense the practice of accounting information manipulation through the use of absolute discretionary accruals is, the greater the adverse effects on price earnings ratio and earnings yield. This is because it introduces bias which hurts the neutrality of accounting information (SFAC 8, 2010). We recommend that regulators should increase scrutiny or constraints over accounting discretion and flexibilities allowed by accounting standard to curtail distortions by financial statement preparers in order to eliminate earnings manipulation and achieve high level of faithful representation.*

**KEYWORDS:** Accounting information quality, Financial Performance, Faithful representation, Price/ earnings ratio, Earnings yield, Nigerian Banks.

## INTRODUCTION

Financial statements are the mediums by which both the internal and external stakeholders gain an understanding about the financial condition and operating performance of the corporations. The accuracy and faithful representation of the accounting information contained in them are

very crucial for all the stakeholders of a corporation to make appropriate decisions. Accounting information is the quantitative and qualitative written information contained in a complete or partial financial statement. These statements include statement of financial position, statement of comprehensive income, statement of cash flow, and other micro and macroeconomic indicators. However, accounting information may be deliberately distorted by the activities of financial statement preparers who wish to alter the content of the data being transmitted due to the flexibility allowed by accounting standards in the recording of transactions, preparation and presentation of financial statements. Accounting flexibility gives firms' management the opportunity to manage earnings aggressively which can eventually evolve to fraudulent practices. Mamo & Aliaz, (2014) asserted that accounting information could be distorted by erroneous presentation and misstatement of the financial position/performance, creating a false impression of an organization's financial strength. It creates information asymmetry for readers of financial statements that affect their decision-making. This opportunistic behaviour found in the arena of financial reporting provides incentives for managers to make decisions in their own interest to the detriment of the firm`s owners, investors, creditors, government and other stakeholders who relied on the such decisions (Fama, 1980; Fama& Jensen, 1983; Badertscher, 2011).

Faithful representation of accounting information is a new concept, which replaces 'reliability' used by the superseded Statement of Financial Accounting Concepts No. 2 (SFAC 2) (FASB 1989). To be useful, accounting information must be faithfully represented. This attribute of faithful representation is achieved when Information has the quality of completeness, neutrality, and freedom from material error and can be depended on by users to represent faithfully that which it purports to represent or could reasonably be expected to represent. Faithful representation assures that financial reports represent economic phenomenon in words and numbers. That is, transactions and events are accounted for in a manner that represents their true economic substance rather than their mere legal form.

The accounting profession continues to struggle with the problem of the veracity of accounting reports, considering the different needs of various financial statement readers for truthful reports. Accounting scandals experienced in the last few years have affected the investors' trust of financial statements. The Enron and Worldcom accounting scandals in the United States, Oceanic bank, Intercontinental bank, and Cadbury crisis in Nigeria all relate to deception. All such scandals involved to varying degrees the telling of accounting untruths, which raises the question; what possible meaning(s) can be given to accounting information being true? Can there be honesty and transparency of accounting information in a business and economic environment alleged to have been characterised with financial engineering and distorted accounting information from notable corporate organizations?

Despite impressive performance on the NSE, available records have shown that information contained in financial statements prepared by DMBs in Nigeria are not allied with its stock market value due to falsification of accounting numbers (SEC, 2013). The falsification of accounting information creates abnormalities in the banks' financial statements particularly and in capital market performance in general. The increasing rate of manipulative accounting information therefore is of huge concern to investors, regulators and other stakeholders because distorted accounting information can cause wrong decisions. The overall effect is wrong share pricing which can cause collapse of capital market, thereby contradicting the basic quality of financial reporting which is assumed to result in more efficient functioning of financial markets

and reduces cost of capital for the reporting entity. This is evident in the near collapse and present lull in the Nigeria capital market. The critical nature of the above problems underscores the imperative of this study which seeks to evaluate the extent to which financial performance of quoted banks in Nigeria could be affected by faithful representation of accounting information (measured by absolute discretionary accruals), towards restoring investors' confidence in banks financial statements and increasing investment in banks stocks in the Nigerian capital market. The above core issues constitute the problems of this study.

Since faithful representation is a new concept as aforementioned, the conceptual framework for financial reporting has not provided a general empirical measure of faithful representation thereby causing paucity of study about faithful representation in Nigeria; this reveals a gap for new study. This study abridges this gap by ascertaining a measure of faithful representation in terms of earnings manipulation and fraudulent behaviours because when earnings manipulation occurs, accounting information does not fulfil the requirement of neutrality. Although similar studies have been carried out in developed economies, in a less developed economy like Nigeria, high level faithful representation of accounting information is probably difficult to achieve in financial reports of banks due to propensity of manipulation and fraudulent accounting practices being the major character traits of weak institutionalized environments. Previous studies were carried out in capital extensive industries like the manufacturing sector and the current work is carried out in the financial sector which is highly regulated. Thus, the nature of industry may affect the result and prevent generalization, hence the need for a new study on the subject. The aim of this study is to empirically investigate the effect of faithful representation of accounting information on the financial performance of quoted banks in Nigeria.

## LITERATURE /THEORETICAL UNDERPINNING

## THEORETICAL FRAMEWORK
The theories which provide support for this study include: Agency Theory, Stakeholders Theory and Positive Accounting Theory.

**Agency Theory:** Agency theory is embedded on the concept of principal-agent relationship wherein a party (principal) defines duties, responsibilities and jobs of the other party (agent), and the agent is expected to discharge the responsibilities entrusted to him by the principal. The investor (principal) engages the services of management (agent), defines terms, conditions of assigned duties, responsibilities and delegates operations of entity to the agents (here the management and directors) to perform tasks or activities that ought to have been performed by the principal. The agency theory proposes or presumes that parties may be self-motivated to pursue self-aggrandizements. This assumption of self-interest dooms agency theory to inevitable inherent conflicts. The self-interested motives by parties lead to deviation of agent from set goal of principal and create conflicts with expectations.

**Stakeholders Theory:** The stakeholder's theory identified stakeholders of a firm, designed models and recommended strategies that should be adopted by management to satisfy diverse parties which have interest in the firm. The stakeholder theory defines organizations as multilateral agreements between the enterprise and its multiple stakeholders and the relationship between the company and its internal and external stakeholders (Jensen, 2001).

Unlike the agency theory that considers the shareholders' interests alone, stakeholder theory considers the interests of all parties in a corporation which are diverse and sensitive to the negative effect of misinformation.

**Positive Accounting Theory:** The Positive Accounting Theory (PAT) aims to proffer explanation and predict actions about how accounting policy choices are made and how firms adjust its activities to new accounting rules while recognizing the existence of economic implications for each choice. The PAT theory may be delineated into Bonus plan hypothesis, Political cost hypothesis and debt/equity hypothesis.

The bonus plan hypothesis states that managers of firms with bonus plans are more likely to use accounting methods that increase current period reported income. Such selection will presumably increase the present value of bonuses if the compensation committee of the board of directors does not adjust for the method chosen. That is, companies by selecting the accounting methods use bonus plans to increase the income of the current period.

The political cost hypothesis predicts that large firms rather than small firms are more likely to use accounting choices that reduce reported profits. High profit can attract increased political pressure in form of higher taxes or stiffer regulations such as amendments to standards of reporting.

The debt/ equity hypothesis states that companies with a higher ratio of debt to equity select the accounting procedures for the transfer of income from future periods to the current period in order to avoid debt covenant violations. It predicts that the higher the firm's debt/equity ratio, the more likely manages use accounting methods that increase income. Managers exercising discretion by choosing income increasing accounting methods to relax debt constraints and reduce the costs of technical default (Watts and Zimmerman, 1990).

## CONCEPTUAL FRAMEWORK

The conceptual framework for this study is developed from the a priori to explain the relationship between the proxies of the explanatory variables (faithful representation of accounting information) and the proxies of the dependent variable (financial performance) which are simply the market-based measures of performance. The conceptual framework as depicted in Figure 1 below is premised on the assumption that there is a nexus (positive/negative) between faithful representation of accounting information and financial performance proxies: Price earnings ratio (PER) and Earnings Yield (ENY).
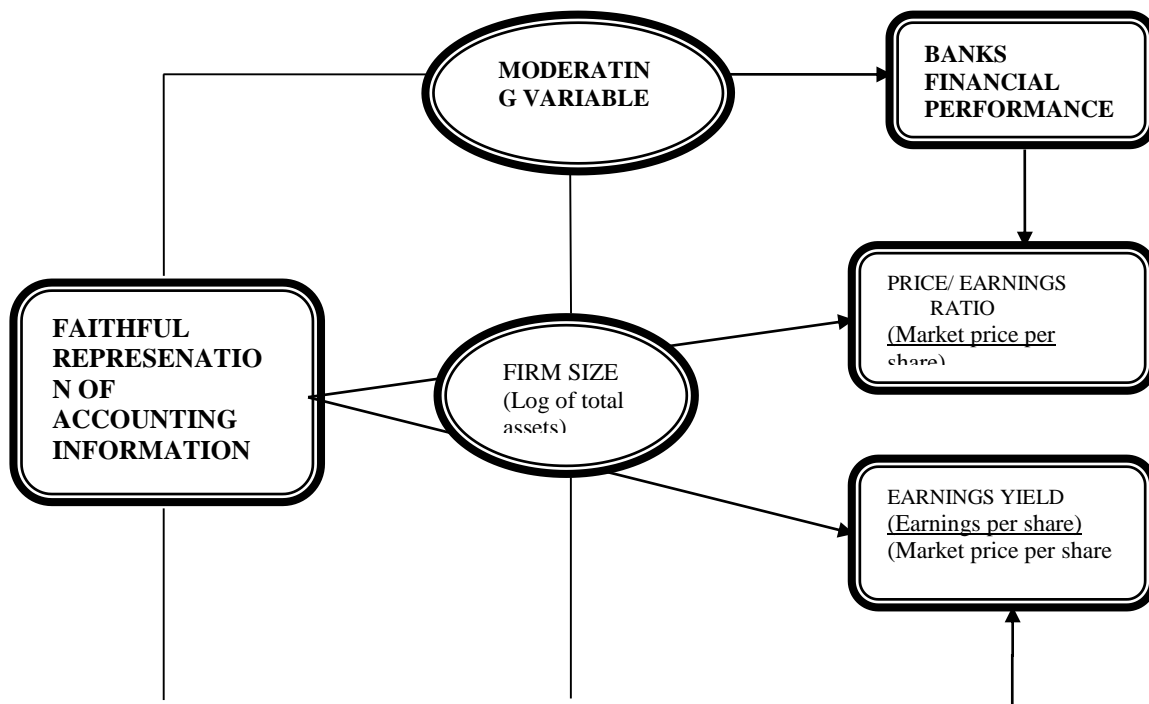
*Fig 1: Operational framework of faithful representation of accounting information and financial performance of Quoted banks in Nigeria- Researcher's Design*

The framework postulates that faithful representation of accounting information (FRAI) could have effect on financial performance proxies. The framework therefore assumes that faithful representation of accounting information (FRAI) could affect DMBs price earnings ratios (PER) positively or negatively. It was therefore hypothesised that "faithful representation of accounting information does not significantly affect the price earnings ratios of quoted banks in Nigeria". The framework also assumes that faithful representation of accounting information (FRAI) could affect DMBs earnings yield hence, we hypothesised that "faithful representation of accounting information does not have a significant effect on earnings yield of quoted banks in Nigeria". Considering the role of size in terms of total assets in measuring the financial performance, we incorporated the variable- firm size in the framework because of its ability of moderating the effect of the independent variable on the dependent variable. Therefore, natural logarithm of total asset was captured in the framework as firm size.

Financial Performance is a measure of how well a firm can use assets from its primary mode of business and generate revenues. This term is also used as a general measure of a firm's overall financial health over a given period. Price to Earnings ratio is the ratio of a company's stock price to the company's earnings per share. It shows the sum of money an investor is ready to pay for each naira worth of the earnings of the company

Earnings yield are the earnings per share for the most recent 12-months period divided by the current market price per share. It is the inverse of the price/ earnings ratio showing the percentage of each naira invested in the stock that was earned by the company.

**Incentives for accounting information distortions**

According to Healy and Wahlen (1998), there are various incentives for accounting information falsification. These incentives impede faithful representation of accounting information. They could be classified broadly into signalling, contracting, capital markets and regulation.

i) **Signaling Incentive:** Managers exploit loopholes to present plausible picture of firm or disclosures of information to stakeholders via financial statements. This creates propensity to manipulate earnings through choices that impacts reports thus creating specific signals about firm. According to Salah (2010), managers will falsify income to convince stakeholders by creating specific signals about firm. This signalling by managers may be upwards swing to outperform competitors, create positive signal or outlook to present worse image of firm. This is essentially such that a worse image currently will produce huge rewards subsequently when performance improves. Subsequent future rise in income may be linked to good result and managers will be rewarded with higher bonuses.

ii) **Contracting incentive:** Contractual obligations help to align firm's interest with expectations of other stakeholders including employees. These contracts rely on accounting data controlled by management. Management rewards are sometimes based on performance tied to financial reports credit contracts agreements are prepared to mitigate managers' actions that favour firm's shareholders to the detriment of credits. These business links between the firm and stakeholders create opportunities for managers to deploy influenced earnings to fulfil contract covenants (Salah, 2010; Healy, 1985; Deschow &Sloan, 1995). Managers can utilize earnings managed results to optimize bonuses or effect compliance with liquidity and solvency clauses embedded in contracts. Compensation contracts and fulfilment of loan covenants are the main motives for earnings modifications (Watts & Zimmerman, 1987).

iii) **Capital market Incentive:** Investors and analysts rely on accounting information to evaluate firms. The fluctuation in share prices creates opportunities for manipulations of financial reports to determine interim share prices (De Angelo, 1988). The suspicion that capital markets motivate earnings alterations is premised on the expectation of deployment of efforts in determining stock prices to derive gains from it. This is possible when gaps exist between accounting information and investors' expectation. Manipulations occur when managers use any strategy to mitigate earnings when average returns are higher or raise earnings during periods of lower returns (Gaver et al, 1995). Managers try to deceive stakeholders through presentation of a stable profit outlook and a plausible firm image. This is based on the belief that constant earnings fluctuations are signals of instability which influence share prices. Therefore, capital market motivation is simply interplay of forces between analysts, management, investors and regulators.

iv) **Regulatory incentive:** Government and financial regulators introduce rules for control of managerial activities, mitigate manipulations and consequently improve accounting quality. Theses create two effects. First it increases potential for motivating managers to modify earnings. For instance, the flexibilities allowed by accounting standards in financial reporting. Second, excessive attention by government and regulators may negatively impact firms' performance. Compliance with regulations mitigates sanctions while defiance increases sanctions. However, managers may devise strategies to circumvent rules and also avoids

sanctions. According to Healy and Wahlen (1999), earnings management may draw the attention of standard setters because of antitrust reasons. This view draws support from Goncharov and Zimmerman (2008) which asserts that governments and market deploy strategies to curtail manipulative behaviours. This can be accomplished using standards, auditing, internal control mechanisms, enforcements and implementation of disclosure requirements for firms in the financial markets.

## EMPIRICAL REVIEW

The lack of faithful representation is often associated with the amount of manipulation exercised by management on financial reporting in terms of falsification and presentation of inaccurate figures. Hosseinian & Ramzani (2016) studied earnings management and profit earnings capacity of firms in Tehran Stock Exchange. The results revealed a significant negative correlation between profitability and earnings management. Debnath, P. (2017) investigated the impact of firm's growth and performance on earnings management in Indian non-financial firms between 2007 and 2015. The results showed a significant positive relationship between firm's growth and earnings management implying that increasing the growth of a firm result in aggressive earnings management.

Gill, Biger, Mand, & Mathur (2013) studied listed manufacturing firms of BSE and the result revealed that the practice of earnings management adversely affects corporate performance and in return lower the market price of share in the long run. Rahmani & Akbari (2013) examined performance coefficients and earnings management. Using multiple correlation analysis, the study found that a negative association existed between performance coefficient and earnings management while positive relation exists between firm's size and earnings management. Akram, Hunjra, Butt & Ijaz (2015) conducted a study on firm performance and earnings management, comparing the Indian BSE listed firms with Pakistani KSE listed firms. The research outcome revealed a negative association of performance and earnings management in Pakistani firms while a positive association was evident in India during period under study. Salim (2012) studied the relationship between bank size and financial performance of commercial banks in Kenya. The main findings of the study established strong correlations between all the studied factors of bank size.

## METHODOLOGY

## DATA
The population consists of all commercial banks in Nigeria. The purposive sampling technique was adopted to select the fifteen (15) quoted banks for the purpose of investigation. Financial statements of the sampled banks between 2007 and 2016 were used for the study.

## VARIABLES

### Independent Variables
The independent variable of this research is faithful representation of accounting information measured by (Absolute Discretionary Accruals) and tested by the cross-sectional modified-Jones model of Dechow et al (1995) which is the difference between net operating accruals and non-discretionary accruals.

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**Dependent Variable**

The dependent variable in the model is financial performance and is proxied by Price earnings ratio (PER) and Earnings Yield (ENY).

**Price to Earnings Ratios (PER):** PE ratio shows the number of times the share price covers the earnings per share over a year. It may also be interpreted as how much an investor pays for every ₦1 naira the bank earns.

**PE ratio = <u>Market price per share</u>**
         **Earnings per share**

**Earnings Yield (ENY):** Earnings yield are the earnings per share for the most recent 12-months period divided by the current market price per share. It is the inverse of the price/ earnings ratio showing the percentage of each naira invested in the stock that was earned by the company.

**ENY =<u>Earnings per share</u>**
     **Market price per share**

**Moderating variable**

**Firm size (FSIZ)** is measured as the natural logarithm of book value of total assets.

**MODEL SPECIFICATION**

Two econometric models were constructed to determine the effect of the independent (predictor) variable on the dependent (criterion) variable in the study. The two proxies of the dependent variable (banks financial performance), price earnings ratio and earnings yield were captured in the models viz-a-viz contemporaneous predictor variable as well as a moderating variable of firm size to evaluate the effect of faithful representation of accounting information on financial performances of quoted banks in Nigeria.

Stemming from the conceptual framework in figure 1, the functional form of the models is stated below:

$$FP \quad = \quad f(ABSDA, FSIZ)$$
$$Fp \quad = \quad PER \text{ and } ENY$$
$$PER \quad = \quad f(ABSDA, FSIZ) \qquad\qquad (i)$$
$$ENY \quad = \quad f(ABSDA, FSIZ) \qquad\qquad (ii)$$

From functional relationship, econometric models are specified thus:
$$PER_{it} \quad = \quad \alpha_0 + \alpha_1 ABSDA_{it} + \alpha_2 FSIZ_{it} + \mu_{1,t} \qquad\qquad (iii)$$
$$ENY_{it} \quad = \quad \beta_0 + \beta_1 ABSDA_{it} + \beta_2 FSIZ_{it} + \mu_{2,t} \qquad\qquad (iv)$$

Where:

PER = Price earnings ratio measured as the ratio of the current market price of share to its EPS

ENY = Earnings yield measured as the ratio of the EPS to the current market price

ABSDA = Absolute discretionary accruals value estimated using modified Jonesmodel (measuring FRAI)

FSIZ = Firm size measured by logarithm of total assets while:

i        = number of banks

t        = period covered in the study

$\alpha_0, \beta_0$=intercepts or constant regression coefficients

$\alpha_1, \beta_1$= slope coefficients or coefficient of intercepts

$\mu_{1,t}$        =        error term

The predictor variable (ABSDA) and moderating variable of FSIZ were included in all the equations with constant regression coefficient ($\alpha_0, \beta_0$), of intercepts ($\alpha_1, \beta_1$,) and the residual error of the regression ($\mu_{1,2}$).

**A priori expectations**
Theoretically, the relationships between variables in the models are summarized as follows:

$\alpha_1, \alpha_2, > 0$

$\beta_1, \beta_2, > 0$

**RESULTS/FINDINGS**

| Statistics | PER | ENY | FRAI | FSIZ |
|---|---|---|---|---|
| Mean | 18.33245 | -0.513068 | 0.010231 | 27.45727 |
| Median | 6.100000 | 0.115000 | - | |
| 1.469344 | 27.57397 | | | |
| Maximum | 932.0000 | 35.36000 | 57.88622 | |
| 30.51824 | | | | |
| Minimum | 29.90000 | -126.3750 | -1.813405 | |
| 22.19175 | | | | |
| Std. Dev | 78.49516 | 15.65709 | 6.859437 | |
| 1.016747 | | | | |
| Skewness | 10.87794 | -6.161360 | 6.341691 | - |
| 0.894527 | | | | |
| Kurtosis | 126.6499 | 51.00771 | 46.34023 | |
| 6.947301 | | | | |
| Jarque-Bera | 96546.09 | 15046.61 | 12490.37 | |
| 115.0391 | | | | |
| p-value | 0.000000 | 0.000000 | 0.000000 | 0.000000 |
| Obs | 150 | 150 | 150 | 150 |

**Table 1: Descriptive Summary of the Data**

*Source: Researcher's estimation using E-views 10.0 output*

The descriptive statistics on table1 indicate that PER has an average value of 18.332 with maximum and minimum values of 932.0 and -29.90 respectively. The standard deviation stood at 78.49516 which is high and the difference between the maximum and minimum values suggest substantial deviations of PER for firms in the sample from the mean. The average ENY is -0.513068 with a maximum value of 35.360 and minimum value of -126.3750 respectively. The standard deviation stood at 15.657 which is high and the difference between maximum and minimum values suggest substantial deviations of ENY for the firms in the sample from the mean. This implies that PER varies significantly across the banks. FRAI has a mean value of 0.01023 with maximum and minimum values of 36.967 and -10.27049 respectively with a standard deviation of 6. 8594. The mean value for FSIZ stood at 27.45727 with maximum and minimum values of 30.5182 and 22.19175 respectively with a standard deviation of 1.016747. The Jacque-Bera statistics for all the variables reveals that the series are normally distributed given that the probability values for the J.B statistics are all less than 0.05. This implies the absence of significant outliers in the data.

The results of analysis of correlation between the variables of study are indicated on the table below:

| | FIRMSIZ | ENY | PER | ABSDA |
|---|---|---|---|---|
| FIRMSIZE | 1 | | | |
| ENY | 0.050123 | 1 | | |
| PER | -0.08285 | 0.00852 | 1 | |
| FRAI | 0.09985 | 0.0058 | -0.0323 | 1 |

**Table 2: Correlation Analysis**
*Source: Researcher's estimation using E-views 10.*

Based on table 2, we observed that FRAI is positively correlated with ENY(r = 0.0058) but negatively correlated with PER(r = -0.0323).The positive correlations indicate that a rise in one variable will be associated with an increase in the other variable and vice-versa. However, correlations are limited in their inferential abilities as they do not necessarily imply causality in a strict sense.

**Hypotheses Testing**

**Ho$_1$:** **Faithful representation of accounting information does not have a significant effect on price earnings ratio of quoted banks in Nigeria.**

| | Aprori sign | RE | FE | FE |
|---|---|---|---|---|
| C | | 18.2494* | 18.8238* | 7.3675 |
| | | (6.2792) | (0.4224) | (17.5731) |
| | | {0.004} | {0.000} | {0.6757} |
| FRAI | | -0.3676 | -0.4658** | -0.26812 |
| | | (0.3528) | (0.2789) | (0.16532) |
| | | {0.2991} | {0.0978} | {0.1073} |
| FIRM | | | | 0.3994 |
| SIZE | | | | (0.6338) |
| | | | | {0.5296} |
| | | Model Parameters | | |
| $R^2$ | | 0.0010 | 0.443 | 0.450 |
| Adj $R^2$ | | -0.005 | 0.382 | 0.1867 |
| F-Stat | | 7.2913 | 5.675 | 6.659 |
| P(f-stat) | | 0.1509 | 0.000 | 0.000 |
| D.W | | 2.25 | 2.2 | 2.1 |
| | | Model Diagnostics | | |
| Hausman | | | 0.0023 | |
| B-G for serial corr. | 0.223 | | | |
| B-P-G for Hetero. | 0.067 | | | |
| Ramsey Test | 0.904 | | | |

**Table 3: The effect of FRAI on PER**

Source: Researchers compilation (2018), ( ) are standard errors; { } are p-values, * sig at 5%

The *p*-value of the Hausman test statistic (0.0023) indicates that the RE method may give bias and inconsistent estimators when compared to FE model and hence the FE estimation is preferred. As shown in the results, the $R^2$ for the FE model is 0.443 which implies that the model explains about 44.3% of the systematic variations in the dependent variable with an adjusted value of 38.2%. The F-stat is 5.67 (p-value=0.00) is significant at 5% and suggest that the hypothesis of a significant linear relationship between the dependent and independent variables cannot be rejected.

The analysis of coefficients reveals that the effect of FRAI on PE-ratio is negative (-0.4658) and significant at 10% {p=0.0978}. As observed from the table, the associated p-value of the t-statistic of FRAI (faithful representation of accounting information) is 0.0978 which is higher than the stated 5%. This leads us not to reject the null hypothesis of no significance effect of faithful representation of accounting information on price earnings ratio. We conclude that there is a negative insignificant effect of faithful representation on price earnings ratio and also a negative correlation between faithful representation and price earnings ratio.

**Ho2:** **Faithful representation of accounting information does not have a significant effect on earnings yield of quoted banks in Nigeria.**

| | Aprori sign | RE | FE | FE |
|---|---|---|---|---|
| C | | -0.5043* | -0.5051* | -0.99205* |
| | | (1.8519) | (0.007) | (0.3996) |
| | | {0.7858} | {0.000} | {0.0143} |
| FRAI | | 0.00901 | -0.00397* | -0.00395* |
| | | (0.0135) | (0.0010) | (0.0011) |
| | | {0.5070} | {0.0002} | {0.0006} |
| FIRM | | | | 0.01757 |
| SIZE | | | | (0.0147) |
| | | | | {0.2351} |
| Model Parameters | | | | |
| $R^2$ | | 0.0000 | 0.2447 | 0.235 |
| Adj $R^2$ | | -0.0067 | 0.1596 | 0.141 |
| F-Stat | | 0.0022 | 2.8734 | 2.509 |
| P(f-stat) | | 0.9619 | 0.0006 | 0.002 |
| D.W | | 2.2` | 2.3 | 2.3 |
| Model Diagnostics | | | | |
| Hausman | | | 0.0119 | |
| B-G for serial corr. | 0.893 | | | |
| B-P-G for Hetero. | 0.554 | | | |
| Ramsey Test | 0.421 | | | |

**Table 4: The effect of FRAI on ENY**

Source: Researchers compilation (2018), ( ) are standard errors; { } are p-values, * sig at 5%

The *p*-value of the Hausman test statistic (0.0119) indicates that the RE method may give bias and inconsistent estimators when compared to FE model and hence the FE estimation is preferred. The $R^2$ for the FE model is 0.2447 which implies that the model explains about 24.47% of the systematic variations in the dependent variable with an adjusted value of 14.1%. The Durbin Watson statistics of 2.3 suggest that the presence of first order stochastic dependence is unlikely in the errors. The F-stat is 2.873 (p-value=0.00) is significant at 5% and suggest that the hypothesis of a significant linear relationship between the dependent and independent variables cannot be rejected.

The analysis of coefficients reveals that the effect of FRAI on Earnings Yield is negative (-0.00397) and significant at 5% {p=0.0002}. Since the associated p-value of the t-statistic of FRAI (faithful representation of accounting information) is 0.0002 which is less than the stated 5%, this leads us to reject the null hypothesis of no significance effect of faithful representation of accounting information on earnings yield. We conclude that there is significant negative effect of faithful representation on earnings yield, although a positive correlation exists between faithful representation and earnings yield.

**Ho$_3$:** **Firm size does not significantly moderate the relationship between faithful representation of accounting information and financial performance of quoted banks in Nigeria.**

Referring to table 3, when firm size as a moderating variable was introduced, the result shows that the $R^2$ for the model rises slightly to 45% and the impact coefficient of FRAI declines to -0.268 but not statistically significant at 5 or 10% (p=0.1073), though the firm size coefficient is positive (0.3994) and not statistically significant (p=0.5296) at 5%. This implies that firm size positively though insignificantly moderates the effect of FRAI on PER

Similarly, from table 4, with the influence of firm size, the result shows that the $R^2$ for the model remained almost stable at approximately 24% and the impact coefficient of FRAI remained unchanged at -0.00395 though still statistically significant (p=0.0006) at 5%. This implies that firm size does not necessarily moderate the effect of FRAI on ENY. This leads us to reject the null hypothesis of no significant effect moderation. We conclude that firm size does not significantly moderate the relationship between faithful representation and financial performance of quoted banks in Nigeria.

## DISCUSSION

There is a downside to the flexibility allowed by accounting standards in the preparation and presentation of accounting information. With this banks exercise discretion on choice of methods thereby giving them the latitude to show only desired result which may not be reflective of actual outcome from the transactions engaged by the firms. Contrary to *priori* expectation, there is a significant negative effect of faithful representation of accounting information (Absolute discretionary accruals) on price earnings ratio (-0.4658). This implies that an increase in discretionary accruals reduces price earnings ratios. The effect is significant at 10% (p-value=0.0978). Our result conforms to findings of some scholars that associates lack of faithful representation with the amount of manipulation exercised by management on financial reporting (Rahmani & Akbari, 2013; Akram, Hunjra, Butt and Ijaz, 2015; Gill, Biger,

Mand, and Mathur, 2013; Hosseinian & Ramzani, 2016). However, the result expectedly disagreed with findings of other previous studies like Omar and Sabur, (2017) and Debnath, P(2017) who documented positive and significant relationship between earnings management and financial performance. Discretional accruals can be used by managers during seasoned offerings of IPOs to inflate the share price to benefit from overvaluation. Our result is in line with Statement of Financial Accounting Concepts No. 8 of 2010 which states that when earnings manipulation takes place, accounting information does not fulfilled the requirement of neutrality which in long run impedes stock market value of firms.

The negative effect of FRAI on earnings yield suggests that the higher the level of earnings management through absolute discretionary accruals, the greater the adverse effects on earnings yield and vice versa. This is consistent with prior study by Rahmani & Akbari, 2013; Akram, Hunjra, Butt & Ijaz (2015); Gill, Biger, Mand, & Mathur (2013).

## IMPLICATION TO RESEARCH AND PRACTICE

The results of this research confirm that the exercise of discretionary accruals by management does not automatically translate to higher financial performance. This disagrees with Debnath, P. (2017) who found a positive association between faithful representation and financial performance through the exercise of discretionary accruals by firm's managers. Also, for the regulators (FRCN, CBN, SEC), practitioners and academics it provides a valuable platform for understanding the drawbacks of accounting discretion and flexibilities allowed by accounting standard so as to curtail the incidence of earnings manipulations which adversely affect the financial performance of quoted banks in Nigeria.

## CONCLUSION

The focus of this study was to empirically investigate the effect of faithful representation of accounting information on financial performance of quoted banks in Nigeria under the panel data framework using secondary data spanning from 2007 to 2016. Our empirical outcome provides evidence that the explanatory power of faithful representation of accounting information affects and influences banks financial performance. We found a significant negative effect of faithful representation of accounting information (Absolute discretionary accruals) on price earnings ratio and earnings yield. Consistent with prior researchers, the study confirms that the use of absolute discretionary accrual introduces bias, which hurts the neutrality of accounting information as required for faithful representation (SFAC 8, 2010).However, the study suggests that our result should not be the taken without further analysis of the motives for managing discretionary accruals and the reinvestment policy of the firm.
From the findings above, the researcher recommend as follows:
1. The regulators (FRCN, CBN, SEC) should increase scrutiny or constraints over accounting discretion and flexibilities allowed by accounting standard to curtail distortions by financial statement preparers in order to eliminate earnings manipulation and achieve high level of faithful representation.

2. Ethical standards should be observed by managers in the preparation and presentation of financial statements in order to ensure that the accounting information contained in financial statements prepared by DMBs in Nigeria are allied with its stock market value.

## FUTURE RESEARCH

The study investigated accrual- based earnings management through the discretionary power of managers in the preparation of financial statements; further study may incorporate real earnings management through the management of physical activities in the manufacturing sector of the economy.

## CONTRIBUTION TO KNOWLEDGE
The study contributes to existing literature in three ways: First, the findings serve as a wake-up call to the standard-setters for an empirical measurement of faithful representation apart from relevance. Secondly, although the conceptual framework for financial reporting has not provided a general empirical measure of faithful representation which have been a majority reason for paucity of study on the subject of faithful representation in Nigeria, we introduce a new measure of faithful representation of accounting information in terms of earnings manipulation and fraudulent behaviour because when earnings manipulation takes place, accounting information does not fulfil the requirement of neutrality which is consistent with SFAC 8, 2010. Thirdly, the study increase knowledge through formulation of an underlying econometric model for accounting information quality and banks' financial performance

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## APPENDIX
## PRICE EARNINGS RATIO RESULTS

Dependent Variable: PER
Method: Panel EGLS (Cross-section weights)
Date: 08/05/18   Time: 23:55
Sample (adjusted): 2008 2016
Periods included: 9
Cross-sections included: 15
Total panel (unbalanced) observations: 131
Iterate coefficients after one-step weighting matrix
Convergence achieved after 12 total coef iterations

| Variable | Coefficient | Std. Error | t-Statistic | Prob. |
|---|---|---|---|---|
| C | 18.82380 | 0.422391 | 44.56486 | 0.0000 |
| FAITHREP | -0.465832 | 0.278930 | -1.670068 | 0.0976 |
| AR(1) | -0.143477 | 0.089047 | -1.611244 | 0.1099 |

### Effects Specification

Cross-section fixed (dummy variables)

### Weighted Statistics

| | | | |
|---|---|---|---|
| R-squared | 0.443374 | Mean dependent var | 75.37044 |
| Adjusted R-squared | 0.365251 | S.D. dependent var | 91.51043 |
| S.E. of regression | 77.95392 | Sum squared resid | 692756.8 |
| F-statistic | 5.675343 | Durbin-Watson stat | 2.151998 |
| Prob(F-statistic) | 0.000000 | | |

### Unweighted Statistics

| | | | |
|---|---|---|---|
| R-squared | 0.150522 | Mean dependent var | 18.80550 |
| Sum squared resid | 754727.5 | Durbin-Watson stat | 2.368516 |

| | |
|---|---|
| Inverted AR Roots | -.14 |

Dependent Variable: PER
Method: Panel EGLS (Cross-section weights)
Date: 08/06/18   Time: 00:09
Sample: 2007 2016
Periods included: 10
Cross-sections included: 15
Total panel (unbalanced) observations: 147
Linear estimation after one-step weighting matrix
White cross-section standard errors & covariance (d.f. corrected)

| Variable | Coefficient | Std. Error | t-Statistic | Prob. |
|---|---|---|---|---|

| | | | | |
|---|---|---|---|---|
| C | 7.367549 | 17.57314 | 0.419251 | 0.6757 |
| FAITHREP | -0.268126 | 0.165321 | -1.621848 | 0.1073 |
| FIRMSIZE | 0.399444 | 0.633793 | 0.630243 | 0.5296 |

### Effects Specification

Cross-section fixed (dummy variables)

### Weighted Statistics

| | | | |
|---|---|---|---|
| R-squared | 0.450455 | Mean dependent var | 69.19626 |
| Adjusted R-squared | 0.382819 | S.D. dependent var | 86.38916 |
| S.E. of regression | 71.33260 | Sum squared resid | 661484.1 |
| F-statistic | 6.659966 | Durbin-Watson stat | 2.082637 |
| Prob(F-statistic) | 0.000000 | | |

### Unweighted Statistics

| | | | |
|---|---|---|---|
| R-squared | 0.121916 | Mean dependent var | 18.33245 |
| Sum squared resid | 789904.6 | Durbin-Watson stat | 2.564151 |

Dependent Variable: PER
Method: Panel EGLS (Cross-section random effects)
Date: 08/06/18   Time: 00:11
Sample: 2007 2016
Periods included: 10
Cross-sections included: 15
Total panel (unbalanced) observations: 148
Swamy and Arora estimator of component variances
White cross-section standard errors & covariance (d.f. corrected)

| Variable | Coefficient | Std. Error | t-Statistic | Prob. |
|---|---|---|---|---|
| C | 18.24935 | 6.279297 | 2.906272 | 0.0042 |
| FAITHREP | -0.367677 | 0.352801 | -1.042166 | 0.2991 |

### Effects Specification

| | | S.D. | Rho |
|---|---|---|---|
| Cross-section random | | 0.000000 | 0.0000 |
| Idiosyncratic random | | 77.05071 | 1.0000 |

### Weighted Statistics

| | | | |
|---|---|---|---|
| R-squared | 0.001033 | Mean dependent var | 18.24939 |
| Adjusted R-squared | -0.005810 | S.D. dependent var | 78.23424 |
| S.E. of regression | 78.46117 | Sum squared resid | 898798.6 |
| F-statistic | 0.150904 | Durbin-Watson stat | 2.250743 |
| Prob(F-statistic) | 0.698239 | | |

Unweighted Statistics

| | | | |
|---|---|---|---|
| R-squared | 0.001033 | Mean dependent var | 18.24939 |
| Sum squared resid | 898798.6 | Durbin-Watson stat | 2.250743 |

Correlated Random Effects - Hausman Test
Equation: Untitled
Test cross-section random effects

| Test Summary | Chi-Sq. Statistic | Chi-Sq. d.f. | Prob. |
|---|---|---|---|
| Cross-section random | 0.491501 | 1 | 0.4833 |

** WARNING: robust standard errors may not be consistent with
assumptions of Hausman test variance calculation.
** WARNING: estimated cross-section random effects variance is
zero.

## EARNINGS YIELD RESULTS

Dependent Variable: ENY
Method: Panel EGLS (Cross-section weights)
Date: 08/06/18   Time: 01:33
Sample: 2007 2016
Periods included: 10
Cross-sections included: 15
Total panel (unbalanced) observations: 149
Linear estimation after one-step weighting matrix
White cross-section standard errors & covariance (d.f. corrected)

| Variable | Coefficient | Std. Error | t-Statistic | Prob. |
|---|---|---|---|---|
| C | -0.505067 | 0.006949 | -72.67801 | 0.0000 |
| FAITHREP | -0.003971 | 0.001039 | -3.821075 | 0.0002 |

Effects Specification

Cross-section fixed (dummy variables)

Weighted Statistics

| | | | |
|---|---|---|---|
| R-squared | 0.244752 | Mean dependent var | 7.037633 |
| Adjusted R-squared | 0.159573 | S.D. dependent var | 17.69159 |
| S.E. of regression | 15.03986 | Sum squared resid | 30084.26 |
| F-statistic | 2.873403 | Durbin-Watson stat | 2.260289 |
| Prob(F-statistic) | 0.000620 | | |

Unweighted Statistics

| | | | |
|---|---|---|---|
| R-squared | 0.105641 | Mean dependent var | -0.505067 |
| Sum squared resid | 32010.69 | Durbin-Watson stat | 2.404628 |

Dependent Variable: ENY
Method: Panel EGLS (Cross-section random effects)
Date: 08/06/18   Time: 01:34
Sample: 2007 2016
Periods included: 10
Cross-sections included: 15
Total panel (unbalanced) observations: 149
Swamy and Arora estimator of component variances
White cross-section standard errors & covariance (d.f. corrected)

| Variable | Coefficient | Std. Error | t-Statistic | Prob. |
|---|---|---|---|---|
| C | -0.504271 | 1.851967 | -0.272290 | 0.7858 |
| FAITHREP | 0.009006 | 0.013538 | 0.665209 | 0.5070 |

| Effects Specification | | | |
|---|---|---|---|
| | | S.D. | Rho |
| Cross-section random | | 2.159731 | 0.0190 |
| Idiosyncratic random | | 15.51374 | 0.9810 |

| Weighted Statistics | | | |
|---|---|---|---|
| R-squared | 0.000016 | Mean dependent var | -0.462126 |
| Adjusted R-squared | -0.006787 | S.D. dependent var | 15.41719 |
| S.E. of regression | 15.46943 | Sum squared resid | 35177.59 |
| F-statistic | 0.002291 | Durbin-Watson stat | 2.188211 |
| Prob(F-statistic) | 0.961891 | | |

| Unweighted Statistics | | | |
|---|---|---|---|
| R-squared | 0.000030 | Mean dependent var | -0.505067 |
| Sum squared resid | 35790.71 | Durbin-Watson stat | 2.150726 |

Dependent Variable: ENY
Method: Panel EGLS (Cross-section weights)
Date: 08/06/18   Time: 01:35
Sample: 2007 2016
Periods included: 10
Cross-sections included: 15
Total panel (unbalanced) observations: 148
Linear estimation after one-step weighting matrix
White cross-section standard errors & covariance (d.f. corrected)

| Variable | Coefficient | Std. Error | t-Statistic | Prob. |
|---|---|---|---|---|

| | | | | |
|---|---|---|---|---|
| C | -0.992054 | 0.399694 | -2.482035 | 0.0143 |
| FAITHREP | -0.003952 | 0.001122 | -3.523498 | 0.0006 |
| FIRMSIZE | 0.017571 | 0.014732 | 1.192726 | 0.2351 |

Effects Specification

Cross-section fixed (dummy variables)

Weighted Statistics

| | | | |
|---|---|---|---|
| R-squared | 0.234592 | Mean dependent var | 6.828859 |
| Adjusted R-squared | 0.141107 | S.D. dependent var | 17.68708 |
| S.E. of regression | 15.12079 | Sum squared resid | 29951.64 |
| F-statistic | 2.509408 | Durbin-Watson stat | 2.253726 |
| Prob(F-statistic) | 0.002214 | | |

Unweighted Statistics

| | | | |
|---|---|---|---|
| R-squared | 0.105632 | Mean dependent var | -0.509601 |
| Sum squared resid | 32010.64 | Durbin-Watson stat | 2.406849 |