GLOBALISATION AND FINANCIAL REPORTING IN NIGERIA

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Abstract

The published Audited Financial Statement (AFS) as the report-card of the operating performance and financial status of corporate entities is recognized globally as the source of significant economic and financial information for strategic investment decisions. Despite the business failure of some high profile organisations and the rising doubt on the reliability of AFS, the release of this document still carry potential wave in the business world. Accounting practice worldwide is localized within each country where there is an established Accounting Standards which ensure uniformity of financial reporting within same geographical territory. With the emergence of a global push in business operation and the rise of international conglomerates in this era of globalisation, a greater need for fairness and mil disclosure in annual financial reports have become one of the major criteria by which corporate governance is judged. In order to achieve a more uniform financial reporting worldwide, accounting professionals have been called upon to incorporate into the current practice new methods of reporting that focus on actual measurement of hidden assets of corporate entities and also to evolve a harmonized accounting treatment of like items across national boundaries. This paper examined the practice of financial reporting in Nigeria in the light of this international call for harmonization and new innovations in global financial reporting.

Introduction

The publication of the Audited Financial Statements (AFS) of corporate entities is a statutory requirement in every nation of the world communities. The need for a legal backing has been for annual publication of financial statement, which was pan of the Joint Stock Company Act of 1844 and the subsequent statistics. In Nigeria, the statutory requirement is entrenched in Companies and Allied Matters Act (CAMA) 1990 Sections 334, 354 and 370 respectively gives the list of items to be included in such financial statements referred to as Annual Returns or Audited Financial Statement as well as the filling of the Annual Returns with the Corporate Affairs Commission. Other statutory or self-regulating independent 'institutions like Securities and Exchange Commission, Federal Inland Revenue Service (FIRS) and Nigerian Stock Exchange also have specific requirements expected to comply with by a well-prepared Audited Financial Statement (AFS) to ensure accuracy, fairness in presentation and reliability.

In the words of Kothari (2004), increased globalisation of financial and product markets has raised the interest of both market participants and regulators in the quality of financial reporting worldwide.

From the days of stewardship reporting, through decision-making concept and the emergency of the call for generally user objectives, AFS has provided annually the information needed to assess the economic relevance of business enterprise. Thus financial information has been the only generally acceptable economic measurement of corporate performance and its financial status at the end of each financial year of individual company consequent upon its operating performance. The aim of this paper is therefore to examine the concept of financial reporting in a globalised world calling for review in the conventional concepts arising from the dynamics of business operating environment of our time (21st century).

Origin, Concepts and Objectives ofConvention.il Financial Reporting

Financial reporting from general view covers all information generated by accounting department on the operating performance of each organisation. A distinction however exists between internal report and external report when considering accounting information. Internal reporting is associated with the provision of information for management purposes while external reporting is used to describe the process by which information is made available to groups other than management.

What is today known as published account or audited financial statement originated from Joint Stock Company Act of 1844 and Limited Liability Act of 1855 in which British Parliament laid the procedure of stewardship reporting in a legal form (Oluwatusin, 2002). Therefore, having its roots in law, the early objectives of Financial Reports were concerned with:

a. Prevention of fraud by the promoters of limited liability companies, and
b. Giving some protection to creditors and shareholders against the possibility of malpractice by company managers.

It is the enactment of these statutes, which made directors answerable to shareholders for their stewardship of the company, and to no other persons. It is for this reason that the financial reporting has traditionally been concerned with the production and communication of information to shareholders.

However, financial reporting practices have been in recent years subject of controversial debate. The root cause of these criticisms stem from a growing gap between what some perceived to be objectives of financial reports and the traditionalist view, which is established by law. This controversy has led to the emergence of three different schools of thoughts, which emphasise different viewpoints on the financial reporting function, viz:

(a) The traditional view of financial reporting based on the concept of stewardship accounting.
(b) The view, which extends the stewardship functions to include the recognition that
shareholders and investors, are decision makers who require information for that purpose.
(c) The modern view that companies should report to a larger class of general users rather than merely to shareholders and investors.

A comprehensive discussion of these views is contained in Olmvalusin (2002). Suffice here however to say that the agitation and contention of each of these views are currently accommodated in the conventional financial reporting practices all over the world.

Three channels through which financial accounting information can affect investments, productivity and value-added of corporate entities have been identified by Bushman and Smith (2003) viz;

(i) To identify promising investment opportunities;
(ii) To discipline managers to direct resources toward projects identified as good and away from projects that primarily benefit managers rather than owners of capital, and to prevent stealing; and (iii)To reduce information asymmetries among
investors.

Firstly, financial accounting information of firms and their competitors aid managers and investors in identifying and evaluating investment opportunities. An absence of reliable and accessible information in an economy impedes the flow of human and financial capital toward sectors that are expected to have high returns and away from sectors with poor prospects.

Secondly, financial accounting systems clearly supply direct information about investment opportunities. For example, managers or potential entrants can identify promising new investment opportunities, acquisition candidates, or strategic innovations on the basis of t'ie profit margins reported by other firms. Financial accounting systems also support the informational role played by stock price. As argued by Black (2000) and Ball (200 i), a strong financial accounting regime focused on credibility and accountability is a prerequisite to the very existence of vibrant securities markets.

Thirdly, financial accounting information enhances economic performance by reducing adverse selection and liquidity risk. A major component of liquidity is adverse selection costs, which are reflected in the bid-ask spread and market impact costs. Firms' pre-commitment to the timely disclosure of high-quality financial accounting information reduces investors' risk of loss from trading with more informed investors, thereby attracting more funds into the capital markets, lowering investors' liquidity risk.

According to Concepts Statement No. 1 of FASB titled Objectives of Financial Reporting by Business Enterprises, three basic objectives of financial reporting are described as stated below:

(a) Financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit, and similar decisions.

(b) Financial reporting should provide information to help present and potential investors and creditors and other users in assessing the amounts, timing, and uncertainty of prospective cash receipts from dividends or interest and the proceeds from the sale, redemption, or maturity of securities or loans.

(c) Financial reporting should provide information about the economic resources of an enterprise, the claims to those resources (obligations of the enterprise to transfer resources to other entities and owners' equity), and the effects of transactions, events, and circumstances that change its resources and claims to those resources.

According to Upton (2001), the last objective is the most relevant here. Financial reporting tries to provide information about economic resources (stuff) and the two groups that hold claims against those economic resources. In doing so, it provides investors, creditors, and the broader capital markets with a feedback mechanism. That is, it helps to confirm or correct prior expectations.

Perceived Shortcomings of General Reporting Structure

Accounting had existed for well over a millennium though the documentation of its practices began about the last decades of 15th century when the publication of Luca Pacioli 1495 A. D. made public the accounting practice of merchants in Athens provinces. However, while the business world has witnessed a lot of fundamental changes, financial reporting has remained the same with due emphasis on:

(i) Historical concepts not future predictive;
(ii) Cost based rather than value oriented;
(hi) Financial focus with no consideration for non-financial;
(iv) Asset evaluating at the total neglect of intangible but core-valued assets of firm;
(v) Emphasising depreciating value not the appreciating value of core corporate assets.

These perceived shortcomings coupled with bankruptcy of some mega business as like Enron, Worldcom, Tyco, Royal Ahold among others have generated heated debate on the reliability of AFS. This loss of credibility in financial reporting has attracted international concern to the point that the International Federation of Accountants (IFAC) commissioned a Task force in October 2002 to look into the issue of Rebuilding Public Confidence in Financial Reporting. The final report of the Task force published in July 2003 recognised that failures of businesses in which deficiencies of financial reporting have figured prominently are not new phenomena. It however went further to state that almost all the high profile failures are the result of the combined effect of failures in business, failures in governance and failures in reporting. The business issue that should be communicated to users of the financial statements is not properly disclosed, governance structures fail to prevent or detect this, and a reporting failure results. As an entity moves closer to business failure, the incentive to distort reporting increases and, therefore, the chance of reporting failure increases.

The report also identified another factor as part of causative of failures in financial reporting.

This is what it refers to as "Environmental Pressures". It stated that all the participants inevitably operate in an environment that places continuous pressure on them. Those pressures, which may be personal, financial or political, will be heightened if they combine or if the checks and balances that the system is supposed to provide fail to operate. On the international scene the Report identified other causative or influential factors as:

(1) Globalisation and cross-border listing;
(2) Regulatory control and standard setting process that is confined to honour national sovereignty;
(3) The organisational structure of large international firm as being a body under common standards but without a common central control. Each national firm being bound by laws of the country in which it operates.

Nevertheless, the relevance of financial reporting to operation of corporate entity and investment decision remains incontrovertible and no subset exists for its existing function.

The Call For A New Orientation in Financial Reporting

The Special Report or FASB authored by Upton (2001) synthesised views acknowledging the call for new orientation in financial reporting. The following are extracts from the views of these international institutions:

(a) **American Institute of Public Accountants:** A Special Committee of the Institute on Financial Reporting set-up in 1991 observed that increased competition and rapid advances in technology are resulting in dramatic changes. To meet users' changing needs, the Committee recommended that business reporting must:

- Provide more information with a forward-looking perspective, including management's plans, opportunities, risks, and measurement uncertainties.
- Focus more on the factors that create longer term value, including non-financial measures indicating how key business processes are performing.
- Better align information reported externally with the information reported to senior management to manage the business.

fb) **Danish Agency for Development** of Trade **and Industry:** In 1998, the Agency carried out a study which describes intellectual capital accounts which should be recognised in the preparation of financial statement in the following four categories, namely human resources, customers, technology and processes. According to Upton (2001), the "accounts" described in the Danish study arc not accounts in the normal bookkeeping sense. They are a collection of non-financial performance measurements.

(c) **Organisation for Economic Cooperation and Development (OECD):** In June 1999, the OECD sponsored a Symposium on Measuring and Reporting Intellectual Capital: Experience, Issues, and Prospects. The Forum Chairman according to Upton (2001) drew the following conclusions:

(i) The process of value creation in companies is changing. There is a need for belter information on intellectual capital, its relation to tangible capital, and its role in value creation. Financial data are evolving, but, alone, present insufficient information.
(ii) International organisations, governments, standards setters and other stake holders should encourage experimentation that would lead to general principles or guidelines for reporting key indicators of intellectual capital and information on value creation. They should systematically monitor and evaluate the results of such experimentation.
(iii) There is broad support for the creation of a framework for voluntary compilation at the enterprise level of a number of key indicators using all possible approaches, including company benchmarking. The framework for reporting should focus on areas that matter most to company performance.

(iv) Employees, suppliers, and customers are involved increasingly in the value creation process. Improvements in reporting should aim to inform them better.

(v) There is a need for better understanding of the innovations in reporting. New approaches are moving towards Internet based real-time reporting; greater availability of information means that more information about a company comes from multiple sources. As a result, more internal information is available externally.

(vi) Businesses are concerned that disclosure of information on intellectual capital and value creation should be useful to business, as well as stakeholders.

(d) **Institute of Chartered Accountants in England and Wales (ICAEW):** In March 2000, the ICAEW published a study authorised by Charles Leadbeater which Economy, proposes three alternative approaches to financial reporting that he labeled incremental, radical, and hybrid:

- The incremental approach seeks gradually to fill in values for the intangible assets, which traditional balance sheets overlook.
- The radical approach is to devise entirely new balance sheets for companies - Intellectual Capital Balance Sheets - which put intangible assets at the heart of the accounts.
- The hybrid approach is the most radical. It would involve far more sweeping changes, not just to the way managers and accountants value intangibles but also the value placed upon them by society as a whole.

Challenges of New Initiatives To Financial Reporting

There appears to be a consensus among international accounting bodies and institutions on the need to adopt other measurements in addition to the current practice in reporting corporate performance. This new initiatives are generally referred to as the new metrics in financial reporting. Table 1 below shows the result of the survey of views of eight of such institutions on the acceptance of such measurements in the preparation of financial statements.

Table 1:

Agency	New Paradigm	New Metrics	Intangible Assets
American Institute of Certified Public Accountants-Special Committee Financial Reporting		X	
Financial Accounting Standards Board Business Reporting Research project		X	
Canadian Institute of Chartered Accountants- Canadian Performance Reporting Initiative	X	X	
Brookings Institution- Understanding Intangible sources of		X	X
Danish Agency for Development of Trade and Industry- Intellectual Capital Accounts		X	
Netherlands Ministry of Economic Affairs- Intangible Assets, Balancing Accounts with knowledge		X	
Organization for Economic Cooperation and Development		X	
Institute of Chartered Accountants in England and Wales- New Measures for the New Economy		X	X

Source: Adopted from Upton, W. S. (2001) in Business and Financial Reporting: Challenges from the New Economy FASB Financial Accounting Series Special Report No. 219-A April, 2001.

The extensive study of Upton (2001) also identified some of these new metrics as follows:

(i) ***Balanced Scorecard:*** Developed by Kaplan and Norton, the Balanced Scorecard is a model for many of the reporting systems now labeled as "intellectual capital." Its designers saw it as a tool for management reporting and companies use it in that role, both in the United States and internationally. While it was not intended for public reporting, one of its creators recently discussed the possibility of using (or even mandating use ot) the Balanced Scorecard in communications with investors and others outside the company.

(ii) ***Skandia AFS:*** The Swedish Insurance Company Skandia has been a leader in promoting understanding of non-financial metrics.

(iii) ***Karl-Erik** Sveiby **and the** Swedish Movement:* In 1988, a small group of service companies and accountants (the KONRAD Group) published "The Invisible Balance Sheet" (Den Osynliga Balansraknigen), that outlined a theory of "intangible assets" described as customer capital, structural capital, and human capital. The report defined a set of 38 key indicators for a "know-how" company, ranging from familiar financial performance indicators (return on capital employed) to more unusual attempts to capture human factors (individual capital in years, sensitivity to defection). Swedish management consultant Karl-Erik Sveiby was the "convenor" of the KONRAD Group and has continued his role as a proponent of what might be considered new-economy metrics. He proposes an "intangible assets monitor."

(iv) ***The Value Creation Index (VCf):*** This is the outcome of a team work of Cap Gemini Ernst & Young Center for Business Innovation, Chris Ittner and David Larcker of the University of Pennsylvania's Wharton School. The group developed the Value Creation Index that attempts to measure the importance of different non-financial metrics in explaining the market value of companies.

The effects these new metrics are the new challenges on future financial reporting has been addressed in the works of Upton Jr. (2001). Nally (2000) identified other challenges on the same issue which includes inter alia as:

- The closure of the expectation gap and broadening the corporate reporting standard.
- The provision of information the market needs to assess value.
- The integration of the explanation of strategy with published financial data. •
- The information in the financial statement is more forward-looking.
- The need to maintain credibility by giving clear and candid statement irrespective of financial performance.
- The presentation of financial report in the language the market understands - a central theme of value reporting.

The Global Economy and the Need For Harmonisation In Financial Reporting

One of the identified major causes of failures in financial reporting is the multiplicity of rules that a multinational company has to obey in the publication of its financial statements. This problem has been exacerbated by the growth driven expansion of major companies seeking new market across the globe. Globalisation as this trend is termed is the integration of world economies through free-How of trade, finances and human capital made possible by the breakthrough in information technology and the integrated global market at the press computer button.

According to Ajayi (2001) globalisation, which is not a new phenomenon, may be defined as the increasing interaction among, and integration of, the activities - especially economic activities -of human societies around the world. This definition contains both a description and a prescription. The description refers to the expansion of international flows of trade, finance, and information into an integrated global market, the prescription refers to the liberalisation of national and global markets in the belief that free flows of trade, finance, and information will produce the best outcome for both economic growth and human welfare.

Whatever may be its benefits and costs, the global trend of economic integration has place major task on financial reporting. Corporate entities seeking expansion into new economies or cross-border listing now demand a degree of harmonization to enable them present common view to their investors across many national boundaries. Import of globalisation on financial reporting includes inter alia:

- Reporting on cross-border listing;
- Consolidation of foreign subsidiaries;
- Compliance with listing requirement of individual countries and the home country of mother-company;
- Harmonization of accounting standards or setting up of neutral standards to be complied with by all;
- Harmonization on disclosures in financial statements;
- Environmental issues in financial reporting - known as "green revolution";
- Sustainable development and social responsibility reporting;
- Key reporting parameter and measurement for e-business, off-shore transactions and other cross border dealings.

Comparative Structure of Financial Reporting of Nigerian and American Companies

Twenty (20) companies each were selected from Nigeria and America - a total of forty (40) companies in all - for this study in order to carry out comparison of information disclosures in their respective financial statements. Financial Statements of the American companies were obtained from Annual Reports Service of WILink Plc. Richmond, USA. Annual Reports of Nigerian companies were selected from samples obtained by the Department for practical teaching to students. The names of the companies selected from each country are:

Nigeria

Union Bank of Nig. Pic.	Totalfinaelf	Prudentbank Plc.
Wema Bank Plc.	Express Discount Ltd.	Afribank Nig. Plc.
Kakawa Discount House	Cornerstone Ins. Plc.	Longman Nig. Plc.
C & I Leasing Plc.		
West Africa Portland Cement		Association Discount House Ltd.
First Securities Discount House Ltd		UACN Property Devt. Co. Plc.
Regency Insurance Company Limited		WAPIC Insurance Plc.
Access Bank Nigeria Plc.		Paterson Zochonis Industries Plc.
UNIC Insurance Plc.		*UBA Bank for Africa Plc.*

AH the above Financial Statements are for the Year Ended 2001, 2002 and 2003.

America

A.E.R.T. Inc.	Macrovision Corporation	Amerada Hess Corporation
FBL Financial Group Inc.	Frequency Electronics Inc.	Reader's Digest Ass. Inc.
Bamwell Industries, Inc.	Oceanic First Fin. Corp.	Sony Corporation
El Paso Electric	Giga-tronics Inc.	Fannie Mae
Dynamic Oil & Gas, Inc.	Stillwater Mining Co.	Ultimate Electronics
Embndge Energy Partners, L. P.	Silgan Holdings Inc.	
General American Investors	AK Steel Holding Corp.	
Universal American Financial Corp.		

All the Above Financial Statements are for the Year Ended 2003

Note: The differences in year have no impact on information disclosure content of AFS covered.

Table 2: Comparative Analysis of Disclosures in Financial Statement Between Nigerian and American Companies

	NIGERIA	AMERICA
Chairman/President Statement	✓	✓
Reports of Directors	✓	✓
Forward looking Statement and Clauses	X	✓
Reports of Auditors	✓	✓
Reports of Audit Committee	✓	X
Management Report	✓	✓
Management Discussion and Analysis	✓	✓
Statement of Accounting Policies	✓	✓
Balance Sheet	✓	✓
Profit and Loss Account	✓	✓
Cash Flow Statement	✓	✓
Notes to the Accounts	Figurative	Discussion with extensive explanation
Statement of Value Added		
Financial History	5 years	5 years
Market Value of Shares and other items of Capital Stock		
Comparative Figures	2 years	3 years
Share Performance or Stock Market	✓	✓
Employee Equity Compensation Plan	X	✓
Pension Scheme/Income Report	X	✓
Selected Quarterly Financial data and Dividend and Market Information (Unaudited)	X	✓
Operating Segment Financial Information	X	✓
Statement of Changes in Shareholder's Equity	X	✓
Liquidity and Capital Resources explanation in Cash flow Statement	X	✓
Management Report (responsibility of Management on the Accuracy of Financial Statements – signed by the Director, MD & FD)	X	✓
Certification Report	X	✓
Audit Committee Report	✓	X
Compliance with Stock Exchange	X	✓

Key: *S* - Exist
X -None existent

Findings

It can be observed from the Table 2 above the following:

1. American companies were more detailed in their financial reports than that of their Nigerian counterparts.
2. AFS of American companies gives more non-financial information than that of Nigerian.
3. The publication of Audit Committee Report was found in AFS of Nigeria companies only. No such statement in the Annual Report of American States.
4. The following extra disclosure in AFS of American companies were not required for Nigerian companies.

(i) Management Report signed by the two Executive Directors accepting the responsibilities for
the accuracy in the Statement presented.

(ii) Certification Report signed by Chief Executive Officer and Chief Financial Official Officer
accepting responsibility for the financial statement filed with the Security and Exchange Commission consequent upon Sarbanes-Oxley Act 2002.

(iii)FormlO-K, which accompanies each financial statement, submitted to Security and Exchange Commission,

(iv) Auditors consent on Form S-8 approving the submission of AFS as annual return to SEC.

5. Statement of changes in Shareholder's equity of American companies presented a detailed record of the movement in shareholders' funds during the year. No such statement in the AFS of Nigerian companies.
6. Nigerian companies employ the direct method of the preparation of the financial statements, while American companies use indirect method. This implies that the Statement of Cash
Flow in the AFS prepared by Nigerian companies is more informative than that of their American counterparts.

Conclusion

This paper has reviewed extensively the major views and opinions of business and academia on the expected new initiatives in financial reporting in this era of globalisation. A comparative analysis of the content of financial reports between companies in Nigeria and America was conducted using the annual reports of forty selected companies. The findings show that the Financial Report of American companies is more detailed than that of Nigeria except in Statement of Cash Flow where the later is more informative. For accounting profession to hold its relevance in future, there is a need to adopt changes which would address the needs of mega business structures of this information oriented and technologically driven market. Notwithstanding the more criticism and suggestion for new reporting measures, conventional approach still has its relevance in fulfilling the core objectives of financial reporting. Developing countries like Nigeria however require an immediate review of existing law and disclosure requirements to align the practice of accounting profession with the changing trend in global economy. An in-depth study which cover all sector of the economy is inevitable to provide the right platform for accounting profession to develop a basis for adjusting on local report in line with expectation of the global economy.

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