Comparative Value Relevance between International Financial Reporting Standards and Nigerian Statement of Accounting Standards

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Abstract

This study compared the value relevance of accounting information under IFRS and under NGAAP. The study used an innovative variant of ex-post facto design called the "same firm-year" design. The study sampled 81 Nigerian quoted companies; and compared value relevance under the two accounting standard regimes using Fisher F-test. The study found that the value relevance of accounting under IFRS is higher than that under NGAAP. Based on the findings, the study concluded that adoption of IFRS in Nigeria has led to increase in value relevance of accounting information hence financial reporting quality. The study recommends that financial statement users' especially investors should have faith in the accounting information presented under IFRS in making economic decisions. The study also recommends that preparers and regulatory authorities should embrace IFRS and perfect their knowledge of it. Finally, it is recommended that organisations in the accounting education supply chain should incorporate IFRS in their study programmes.

Keywords: IFRS Adoption, NGAAP, Value Relevance

1.   INTRODUCTION

With the increasing rate of globalization, Foreign Direct Investment (FDI), cross border listing of companies and multinational corporations; there is a heightened need for a common accounting language for financial reporting. It should be obvious; the use of different accounting standards by different nations would and has resulted to several diversities in accounting (Wiecek & Young, 2010). The advent of the International Financial Reporting Standards (IFRS) has served the need for a common financial reporting language by multinational enterprises and providing the comparability of accounting figures required by investors. These realisations have persuaded many nations of the world to converge their national accounting standards to international standards.

The movement towards convergence of the national accounting standards began formally in 1979 with the creation of the International Accounting Standards Committee (IASC) which later became the International Accounting Standard Board (IASB) in 2001. The objectives of the IASB were to develop and promote the application of accounting standards (IFRS) that can be applicable worldwide (IASB, 2010, Preface). In Nigeria, the conversion from the Nigerian local standards, known as Statement of Accounting Standards (hereafter refer to as NGAAP) to IFRS was done in three phases: (i) all publicly listed entities and significant public interest entities migrated to IFRS from January 1, 2012; (ii) all other public interest entities migrated to the international standards from January 1, 2013; and (iii) the Small and Medium Scale Enterprises (SMEs) adopted IFRS for SMEs from January 1, 2014.

Although the NGAAP is similar to IFRS in certain respects, many differences exist (KPMG, 2010). These differences can be significant and have enterprise wide implications. The different nature of the two standards has made it paramount for an empirical study to ascertain whether the adoption of IFRS by Nigerian firms has led to a significant change in the accounting quality measured by value relevance. The requirements of IFRS 1 made this kind of study possible in the first year of IFRS adoption using the statements of reconciliation from NGAAP to IFRS.

The purpose of this study is therefore to compare the value relevance of accounting information under IFRS with the value relevance of accounting information under NGAAP. The paper is in five sections: Section 1 introduced the paper, section 2 is a literature review in which the key concepts investigated by the study are clarified; section 3 explains the methodology adopted in the paper; section 4 presents and analyses the results of the study, and finally, conclusion and recommendations are contained in section 5.

2.   LITERATURE REVIEW
2.1   Conceptual clarifications

Two concepts are important to this study: value relevance and accounting standards. Value relevance has several definitions, including the ability of accounting information to be captured in share prices - the measurement a view (Ohlson, 1995); the ability of the accounting information to predict future events such as earnings, bankruptcy, stock returns and so on - the prediction view (Altman, 1965); the information content of accounting data - the information view (Ball & Brown 1968), and the ability to trade on the basis of accounting information

with an abnormal returns- the fundamental view of value relevance (Ou & Penman,1989).

In this paper, financial statements are value relevant if accounting numbers contained in them relate highly to the current market value of the firm. In other words, value relevance refers to the degree to which accounting information is impounded in the security prices. If there is no association between accounting numbers and share prices; then accounting information cannot be termed value relevant, and hence, financial statements are unable to fulfil one of its primary objectives (relevance).

The second concept discussed in this paper is accounting standard. Accounting standard is defined as an information system through which financial and monetized information is generated for economic and political decisions. Statements of accounting standards are developed to ensure a high degree of standardisation in published financial statements. They depict how information should be measured and reported in the financial reports to enhance quality. The two accounting standards used in this study are the IFRS which are mandatorily in force in Nigeria effective January 1st 2012 and the NGAAP that were in force in Nigeria before IFRS adoption. This study therefore examined the extent to which value relevance of accounting information differs under the two accounting standards (IFRS vs. NGAAP) in Nigeria.

2.2   Review of empirical studies

Assessing the relative informativeness of different accounting standard sets has always been of great importance to the policy debate. The main recurring theme in this research area is the market reaction to different accounting standards in order to rank their usefulness for investors. The starting point of the analysis of the impact of IFRS adoption on value relevance was to verify the usefulness of Form 20‐F, which included reconciliation of earnings and book value to US GAAP from other accounting standards. Previous studies such as Barth Landsman and Lang (2008) and Iatridis (2010) stated that IFRS is a more quality standard, and shareholder orientated than national accounting standards in several countries (Tsalvoustas, 2009). On the basis of this claim, several researchers have compared the value relevance of accounting information under IFRS with many other national accounting standards (Horton & Serafeim, 2007; Hung & Subramanyam, 2007; Chalmers, Clinch and Godfrey, 2008 among others).

Recent studies found mixed results on the impact of IFRS adoption on value relevance of accounting information. Using time series analysis and a returns-earnings model, Bartov Goldberg and Kim (2005) found that the value relevance of earnings increased for their sample of German firms that voluntarily switched from German GAAP to IFRS. Similar results were reported by Jermakowicz, Prather-Kinsey and Wulf (2007) regarding 30 German companies listed on the Deutsche Börse with the largest market capitalisation and turnover. Hung and Subramanyam (2007) also examined the value relevance of summary accounting measures, namely the book value and net income, under IFRS and German accounting standard (*Handelsgesetzbuch*-HGB) using "same-firm year design." They found that accounting quality (value relevance) improved under IFRS. Specifically, the book value of equity coefficient was found to be significantly larger under IFRS than under HGB, but, they did not find evidence that the combined value relevance of book value of equity and earnings for their sample of German firms adopting IFRS was significantly higher.

Christensen, Lee and Walker (2007, 2009) used a United Kingdom sample and found that (i) in spite of IFRS being relatively similar to UK-GAAP; IFRS reconciliations still contained information that analysts considered relevant for firm valuation and that (ii) firms opportunistically tended to delay unfavourable reconciliations. Using abnormal returns model, they also found significant market reactions to IFRS reconciliation announcements. Iatridis (2010) also conducted a study of UK firms that switched from UK GAAP to IFRS. The result of his study showed that implementations of IFRS generally reinforce accounting quality and led to more value relevance in accounting measures.

Horton and Serafeim (2007) found that in the UK, French and Italy earnings reconciliations on transition to mandatory IFRS adoption were incrementally value relevant. Horton and Serafeim (2010) confirm that reconciliation adjustments from UK GAAP to IFRS alter investors' beliefs about share prices of firms listed on the London Stock Exchange. The IFRS earnings coefficient was higher and the earnings reconciliation items exhibited incremental value relevance over UK GAAP earnings. Daske, Hail, Leuz and Verdi (2008) noted an increase in value relevance of accounting in equity valuations when firms use IFRS prior to the official adoption date. The study of Bellas Toudas and Papadatos (2008) also examined the issue of value relevance of accounting information after the adoption of IFRS in Greece. They found book value of equity as well as reconciliation of net profit to be more value relevant under IFRS.

Chalmers, Clinch and Godfrey (2008) report no significant increase in the value relevance of combined earnings and book value of equity using IFRS information relative to local GAAP information for a sample of Australian firms. Likewise, Gjerde, Knivsfla and Saettan (2008) investigate Norwegian firms' restatements and found a contrary result. Horton, Serafeim and Serafeim (2008) also found an informational value increase from the reconciliation statements of UK firms upon IFRS adoption.

Clarkson, Hanna, Richardson and Thompson (2008) found a minor change in value relevance for code

law countries and a decrease in value relevance in common law countries. Clarkson et al. (2011) confirm the impact of mandatory IFRS adoption on value relevance both in Europe and Australia by introducing into the pricing model a cross‑product term, equal to the product of earnings and book value, which was intended to reflect measurement errors in accounting variables. They found that including the product term into the regression changed inference; and after controlling for nonlinearities, no difference in value relevance was found between domestic standards and IFRS. Their study shared a similar finding with Goodwin and Ahmed (2006) and Goodwin, Ahmed and Heaney (2008).

Although the literature on the effects of IFRS adoption around the world is bountiful and has grown at an astronomic rate over the past few years, it is subject to certain criticism which we found from the review of prior studies. One of the major gaps identified from the extant literature is the lack of a theory that can guide the managers on how to select the accounting policies, standards and the level of disclosure in the financial statements. Furthermore, most of the prior studies reviewed are not a single country analysis. This present paper is closest to Hung and Subramanyam (2007) in terms of the methodology adopted. They also make a case for a country-specific approach, which considers the direct effects of adopting IFRS for the same set of firm years. Such an approach would help to overcome problems associated with comparing across countries with different institutional arrangements, as well as controlling for time-series differences. Hung and Subramanyam (2007) are only able to observe "book value" reconciliation information (i.e. equity adjustments) for 57 firms; and "net income" reconciliation (i.e. profit at end of prior period adjustments) for 31 firms. Our study covers a sample of 81 firms. Also, the investigation period for this paper is more current than Hung and Subramanyam (2007). As noted earlier, this is important in view of the significant and on-going amendments to IFRS since the "stable platform" was achieved from 2012 in Nigeria.

3.   METHODOLOGY

This study employs an innovative variant of ex-post facto design known as "same firm-year" research design similar to Clearkson et al. (2011), and Hung and Subramanyam (2007) wherein the study documents how IFRS adoption changes the value relevance metrics. Same firm-year research design is a design that varies the reporting GAAP in the same firm(s) and the time period. By implementing this design, the study first analyses the differences in value relevance metrics calculated under IFRS and NGAAP for the same sets of firms and time period, and then testing the statistical significances of the differences.

The population of the study comprises of all the 188 firms listed on the Nigerian Stock Exchange as at 31st December, 2010. The usable sample size used in the study comprises of 81 listed companies using the procedure presented in Table 1. The procedure for the sample size selection is presented in Table 1.

Table 1: The sample selection criteria

Selection Criteria	Number of Firms
Total number of companies listed on the NSE on 31/12/2010	188
Companies delisted from NSE after 31/12/2010	(28)
Companies that do not have their financial statements on NSE website	(27)
Companies yet to publish the 2012 financial statements as at 31/12/2013	(15)
Early IFRS adopters	(6)
Companies that do not present the reconciliation statements	(31)
Sample size	**81**

Source: *Researchers' computation*

The selection of a company as an IFRS adopter is only made once an explicit and unreserved statement of compliance is made in the firm's auditor's report. As can be seen in Table 1; from the initial population of 188 listed firms in Nigeria as at 31st December 2010, 81 listed firms formed a working population. Since the new population is not too large for the researcher to handle all the 81 firms were used as the sample size. The variables used in the study are summarised in Table 2.

Table 2: A Summary of Variables Used

Variables		Proxy	Measurement
Dependent	Share prices	MVS	Measured by the market value of equity share 90 days after year end date of the company.
Independent	1) Earnings reconciliation adjustments	$EPS^{IFRS-SAS}$	Measured by the difference between the net earnings per share under IFRS and NGAAP.
	2) Book value of equity reconciliation adjustments	$BVS^{IFRS-SAS}$	Measured by the difference between the shareholders fund in per share under IFRS and NGAAP.
Control	1) Earnings under NGAAP	EPS^{SAS}	Measured by the earnings per share under NGAAP.
	2) Book value of equity under NGAAP	BVS^{SAS}	Measured by the book value of equity under NGAAP per share.

Source: *Researchers' computation*

Value relevance of accounting information under IFRS or NGAAP is estimated by the association between stock prices and accounting information. The value relevance estimation is done using the Models in Table 3.

Table 3: A Summary of Value Relevance Models under NGAAP and IFRS

VARIABLES	Measures	Measurement
Value relevance under SAS	R_r^2	$MVS_{t+90} = a + \beta_1 EPS^{SAS} + \beta_2 BVS^{SAS}$
Value relevance under IFRS	R_f^2	$MVS_{t+90} = a + \beta_1 EPS^{SAS} + \beta_2 BVS^{SAS} + \beta_3 EPS^{IFRS\text{-}SAS} + \beta_4 BVS^{IFRS\text{-}SAS} + e$

Source: *Researchers' computation*

Where:

MVS_{t+90} = the market value of shares of the firm after 90 days of financial year end (*t*)

EPS^{SAS} = the Earnings per share of firm under NGAAP as at the period *t*

BVS^{SAS} = the Book Value per share of firm under NGAAP as at the period *t*

$EPS^{IFRS\text{-}SAS}$ = the difference between Earnings per share under NGAAP and IFRS of the firm as at the period *t*

$BVS^{IFRS\text{-}SAS}$ = the difference between Book Value of equity per share under NGAAP and IFRS of the firm as at the period *t*

$\beta_1 \ldots \beta_4$ = coefficient of EPS^{SAS}, BVS^{SAS}, $EPS^{IFRS\text{-}SAS}$, $BVS^{IFRS\text{-}SAS}$ respectively

α = the intercept

t = year end date

ε = error term

The first was a control model containing only earnings and book values of equity under NGAAP. The second was an extension of the control model which additionally includes the reconciliation adjustments of book values of earnings and equity from the NGAAP figures to the first IFRS financial statements as required by IFRS 1 to see the extent to which such adjustments are incrementally value-relevant to investors.

Running the above model using forward method enabled us to compare the value relevance of accounting under NGAAP with the value relevance of accounting under IFRS. Where there were no incremental value relevance from the adjustments of earnings and book values of equity in the reconciliation statement in the first IFRS statements then $\beta_3 = \beta_4 = 0$. We predicted positive coefficients for IFRS reconciliation adjustments (i.e., β_3 and/or β_4 with p <0.05). The model used was that by Pope and Wang (2000), Cahan, Courtenay, Gronewoller and Upton (2000). To check the significance of the difference in value relevance under IFRS and NGAAP, the Fisher F-ratio was used. The Fisher F-ratio is calculated as follows:

$$F_{(f-r, N-f-1)} = \frac{(N - f - 1)(R_f^2 - R_r^2)}{(f - r)(1 - R_f^2)}$$

Where

R_f^2 = R² for the full model (value relevance under IFRS)

R_r^2 = R² for the reduced model (value relevance under NGAAP)

f = number of predictors in the full model

r = number of predictors in the reduced model

N = number of observations

4.   DATA ANALYSIS AND RESULTS

Both pre-estimation and post-estimation tests were carried out to ensure that the results emanating from the data are robust to generate reliable coefficients. First pre-estimation check was the deflation of the earnings and book values together with their respective reconciliations to IFRS by the number of shares outstanding on the balance sheet date in order to reduce the size effect on the results. This is similar to other prior studies such as Gjerde et al. (2008) and Clarkson et al. (2011). Furthermore multiple regressions are a parametric tool hence appropriate for use only when an assumption of normality was achieved. Logarithm transformation was done to correct for normality. Afterwards, the formal estimation test was conducted using skewness to check for the normality of our data. The skewness values ranged from -0.118 to 0.533. Since the values of skewness fell within the range of ±2S.E (i.e., ±0.534), the data was judged to be normally distributed. Low correlation coefficients ranging from 0.005 to 0.363 as shown in Table 4 suggest lack of multi collinearity among the variables.

Table 4: Correlation Coefficients between Predictor Variables

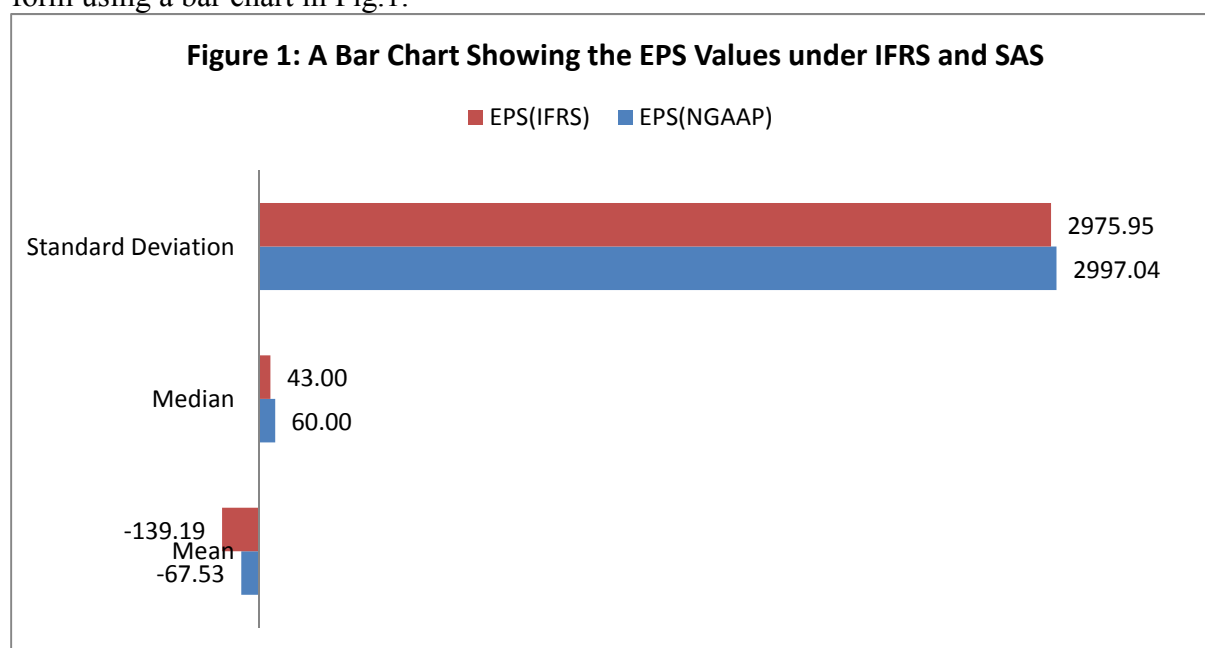| Variables	EPS^{SAS}	BVS^{SAS}	$EPS^{IFRS-SAS}$	$BVS^{IFRS-SAS}$
EPS^{SAS}	1.000			
BVS^{SAS}	0.250	1.000		
$EPS^{IFRS-SAS}$	0.346	0.036	1.000	
$BVS^{IFRS-SAS}$	0.005	0.363	0.230	1.000
N	81	81	81	81

Source: *Researchers' computation*

Finally, Durbin-Watson (DW) test was used for first order autocorrelation. The d_L =1.550, d_U = 1.747 (values obtained from DW table). Since DW (1.840) > d_U(1.747) the errors were assumed not to be positively correlated in the first order autocorrelation.

Table 5: Descriptive statistics of Accounting Measures and their Reconciliation to IFRS

	MVS	EPS^{SAS}	EPS^{IFRS}	$EPS^{IFRS-SAS}$	BVS^{SAS}	BVS^{IFRS}	$BVS^{IFRS-SAS}$
Mean	33.52	-67.53	-139.19	71.66	827.25	883.36	-56.11
Median	4.78	60.00	43.00	2.09	360.22	355.52	2.92
Standard Dev	116.14	2997.04	2975.95	531.49	1628.69	1630.97	358.45
Minimum	0.50	-26026.27	-26026.27	-1377.00	-1073.52	-654.28	-2133.10
Maximum	990.49	3951.00	2200.00	3600.00	11602.77	11083.01	519.75

Source: *Researchers' Computation*

Table 5 reports the descriptive statistics for the EPS and BVS under both IFRS and NGAAP together with the reconciliation figures to IFRS. According to the statistics the mean values of EPS under NGAAP for the 81 sampled listed firms is 68 kobo[1] (loss) while that under IFRS was 139 Kobo (loss). The similar effect is shown by the median whose values are 60 kobo and 43 kobo under NGAAP and IFRS respectively. This is an indication that IFRS are more conservative in profit measurement than the NGAAP. This information is shown in a pictorial form using a bar chart in Fig.1.

Figure 1: A Bar Chart Showing the EPS Values under IFRS and SAS

- EPS(IFRS)   EPS(NGAAP)

Standard Deviation	2975.95 / 2997.04
Median	43.00 / 60.00
Mean	-139.19 / -67.53

The bar chart shows a downward valuation of profitability in Nigeria upon IFRS adoption. On average

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[1] Naira (₦) is Nigerian currency. 100 kobo = ₦1

Nigerian listed firms experienced a reduction in EPS by 72 kobo. In relation to earnings quality the interpretation of these reductions is that IFRS financial statements are associated with more timely loss recognition hence of higher quality because of their quicker reporting of the risk (loss) associated with the investment in a firm.

On the other hand, the BVS of Nigerian listed firms has increased by 56 kobo on average. Using NGAAP the sampled firms reported a BVS of 827 kobo while the BVS of the same firms for the same period was valued on average as 883 kobo under IFRS. This is shown in Fig. 2.

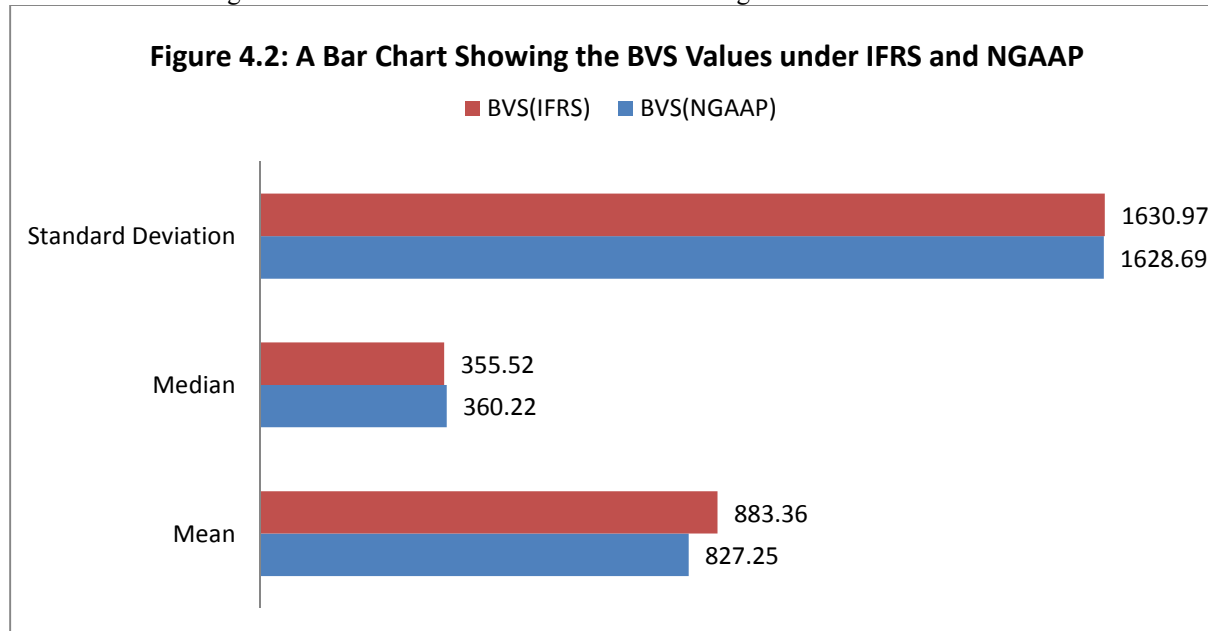Figure 4.2: A Bar Chart Showing the BVS Values under IFRS and NGAAP

Fig. 2 depicts an opposite effect on the BVS of Nigerian listed firms; the figure suggests the IFRS resulted to increase in BVS upon IFRS adoption in Nigeria.

The result from the analysis is presented in Table 6.

Table 6: Value Relevance of accounting under NGAAP and IFRS in Nigeria

	NGAAP	IFRS
Constant	-2.616^{***}	-2.435^{***}
EPS^{SAS}	0.547^{***}	0.448^{***}
BVS^{SAS}	0.265^{***}	0.369^{***}
$EPS^{IFRS-SAS}$		0.198^{**}
$BVS^{IFRS-SAS}$		0.167^{*}
R^2	41.4%	47.7%
F	27.537^{***}	17.312^{***}
ΔR^2		6.3%
ΔF		10.223

$^{*}P < 0.05$, $^{**}P < 0.02$, $^{***}P < 0.01$

With four potential predictor variables, the procedure iterated was through two steps. In the first step, the variable EPS^{SAS} and BVS^{SAS} was included in the model. The final model includes $EPS^{IFRS-SAS}$ and $BVS^{IFRS-SAS}$ to determine if value relevance metric has increased significantly. From Table 6 it can be observed that the inclusion of $EPS^{IFRS-SAS}$ and $BVS^{IFRS-SAS}$ in the second model resulted to higher explanatory power of the model.

The first model without IFRS reconciliation produced ANOVA ($F (2,78) = 27.537$, $p < 0.01$, while the second containing IFRS reconciliations has ANOVA ($F (4,76) = 17.312$, $p < 0.01$). These results indicate that both models are well fitted. In terms of variability in observed share prices accounted for by accounting information under IFRS and NGAAP, the explanatory power of accounting variables increased from 41.4% under NGAAP to 47.7% under IFRS representing a 6.3% increase in value relevance upon IFRS adoption in Nigeria. The coefficients of each independent variable are stated in Table 6; the values with asterisk signs (*) indicate that the t-values of such coefficient take a value different from the statistically significant confidence

level. The coefficients are used to formulate the regression equation below:

$$MVS_{t+90} = -2.435 + 0.448EPS^{SAS} + 0.369BVS^{SAS} + 0.198EPS^{IFRS-SAS} + 0.167BVS^{IFRS-SAS}$$

As explained in section 3, values with triple asterisk (***) indicate that the coefficient is significant at 1%, values with double asterisks (**) indicate that a value significant at 2%; finally, values with a single asterisk (*) show a value significant at 5%. Consistent with our predictions in section 3 the coefficient values of reconciliation adjustments during conversion to IFRS are positive and significantly different from zero; suggesting an increase of accounting value relevance upon adoption of IFRS in Nigeria. We therefore conclude that a mandatory earnings and book value of equity reconciliation adjustments in the first IFRS financial statements is incrementally value-relevant.

To test whether the combined effect of mandatory IFRS adoption has led to a significant change in value relevance of accounting information in Nigeria, the Fisher F-ratio adopted from Howell (2002) was used:

$$F_{(f-r, N-f-1)} = \frac{(N-f-1)(R_f^2 - R_r^2)}{(f-r)(1-R_f^2)}$$

$$F_{(2,76)} = \frac{(81-4-1)(0.477-0.414)}{(4-2)(1-0.477)}$$

$$= \frac{4.788}{1-046}$$

$$= 4.58$$

Since the calculated F-ratio of 4.58 is less than 19.5 the critical value for F, the study concluded that the combined effect of mandatory IFRS financial statement is not significantly different from the value relevance of financial statements under NGAAP.

The findings of this paper are consistent with expectations and prior studies like Horton and Serafeim (2008) who both found positive and significant coefficients of earnings reconciliation adjustments and book value of equity reconciliation adjustments prepare on the conversion to IFRS. This finding is also comparable to Sami and Zhou (2004) in China, Hung and Subramanyam (2007) in Germany, Chalmers et al. (2009, 2011) in Australia, Gjerde et al. (2008) in Norway, Christensen et al. (2007, 2009) in UK and Clarkson et al. (2011) in 15 countries including Australia.

5.   CONCLUS ION AND RECOMMENDATIONS

Based on these findings, the study concluded that the adoption of IFRS did not distort the value relevance of accounting information in Nigeria. In terms of quality, this study concluded that the adoption of IFRS by Nigerian listed firms has led to a 6.7% increase in accounting quality in Nigeria. The study recommends that financial statement users, especially investors, should have faith in the accounting information presented under IFRS in making economic decisions in spite of the fact that the standards (IFRS) are relatively new in Nigeria since they do not distort the value relevance or the quality of accounting information in the country. Furthermore, the National Universities Commission (NUC) and other bodies responsible for setting curriculum for institutions of learning should review the curriculum of the accounting degree or other accounting programmes in Nigerian institutions in order to incorporate IFRS into the syllabus.

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