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FIRM STRUCTURAL TRAITS AND QUALITY OF FINANCIAL REPORTING OF LISTED NON-FINANCIAL FIRMS IN NIGERIA

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ABSTRACT

The presentation of financial reports by firms is becoming a formality because some of the happenings in many firms negate their reports. This study explored the influence of firm structural traits: firm size as well as leverage on the quality of financial reporting of listed non-financial firms in Nigeria. This study adopted the longitudinal (panel) research design. The study utilized the data gathered from listed 72 sampled firms on the Nigeria Stock Exchange from 2012 to 2020; and was analyzed using fixed effect panel regression based on the outcome of different specification tests conducted. The quality of financial reporting was proxy with discretionary accrual. The findings revealed that leverage has a negative significant influence on the quality of financial reporting of listed non-financial firms. Besides, the results indicate that firm size positively and significantly influence the quality of financial reporting of listed non-financial firms. Hence, the study recommends that leverage should be made optimal by firms so as to limit their exposure pressure of having to engage in earning management while trying to assure creditors of the firm's ability to repay the loans.

Keywords: quality of financial reporting, firm traits, firm size, leverage

INTRODUCTION

The presentation of financial reports by firms is becoming a formality because some of the happenings in many firms negate their reports; in this wise, the quality of financial reporting is questionable. Financial reports are a formal and complete statement describing the financial happenings of business entities. In order to make the financial statement transparent, the presentation should not be deceptive while the user can comprehend the presented information without much effort (IASB, 2008).

The higher the quality of financial reporting, the more important are the advantages earned by investors and users of financial reports (Herath & Albarqi, 2017). Consequently, over the years, the accounting scandals that took place in foreign financial institutions and Nigeria have raised questions and worries regarding the quality of financial reporting (Agrawal & Chadha, 2005; Brown et al., 2008). Notable firms like Marconi, Worldcom, Enron, Parmalat, Cadbury, and Bank Oceanic have engaged in financial fraud; this reduced the confidence of investors in the management and their published financial reports (Biddle et al., 2009).

Firm traits are described as a firm demographical and managerial variable which in turn, include group within the firm's domain Zou & Stan, 1998 as cited in (Egbunike & Okerekeoti, 2018). These traits cannot be overemphasized because of their importance in determining the quality of financial reporting. There are seven independent variables which were chosen as substitutes for the firm's trait such as: firm growth, profitability, institutional shareholding, liquidity, board composition, leverage, and firm size. They were further re-grouped into three, namely: structure variables such as firm size and leverage; monitoring variables are boards' composition and institutional shareholding; while performance variables are profitability and liquidity (Hassan & Bello, 2013).

Several studies were done on structural variables and quality of financial reporting revealing a positively strong and significant association between firm size and quality of financial reporting of non-financial firms listed (Agyei-Mensah, 2014; Al & Ahmed, 2012; Asegdew, 2016; Hossain et al., 2012). Egbunike & Okerekeoti, (2018) revealed that, the firm traits: firm size, and leverage were significant while Olowokure et al., (2015) showed that firm size, leverage, and the quality of financial reporting were not significantly related.

Given, the aforementioned problem and findings by several studies that have been undertaken on this topic; Hassan & Bello, (2013) submitted a detailed report that firm traits influence quality of financial reporting of non-financial firms listed in Nigeria, others are; (Okunbor & Dabor, 2018; Egbunike & Okerekeoti, 2018).

Statement of the problem

Despite numerous measures from foreign financial institutions to strengthen the standard of financial reporting; that reached the peak at the beginning of International Financial Reporting Standards (IFRS) and its succeeding acceptance alongside a meaningful number of nations, the wave of firm offense and fraud was retained on a universal extent. Particularly, in 2014, after examination; Glaxo Smith Kline (GSK) engaged in extensive global corruption reaching £320m as a result of the low quality of the financial report (Okunbor & Dabor, 2018). Also, in 2015, the Financial Reporting Council of Nigeria suspended the Chairman, two directors and the CEO of Stanbic IBTC Bank for filing false financial statements between 2013 and 2014 affirmed this and also shows that the regulator takes the quality of financial reporting issue seriously.

In Nigeria, financial reports are controlled by regulations and standards from different authorized financial regulatory entities like the Financial Accounting Reporting Council of Nigeria (FRC), the Securities and Exchange Commission (SEC), Nigeria Stock Exchange (NSE) to say a few (Olowokure et al., (2015). Concerning firm traits as well as the quality of financial reporting, many works have focused on few non-financial firms listed. Therefore, this study filled the gap of considering the influence of firm structural traits on quality of financial reporting of listed non-financial firms in Nigeria from 2012 - 2020. The broad objective is firm structural traits influence on quality of financial reporting of listed non-financial firms in Nigeria; while the specific objectives are: to examine the relationship between firm size and quality of financial reporting of listed non-financial firms in Nigeria; as well as to evaluate the relationship between leverage and quality of financial reporting of listed non-financial firms in Nigeria.

LITERATURE REVIEW

Quality of Financial Reporting

Alwardat, (2019) stated that the standard of financial reporting is an essential trait of financial reports. The reliance of investors in the reliability of these reports and whether they show the truth as regard the accomplishments of a publicly held firm affect their insight and dictate their business resolutions. Egbunike and Okerekeoti, (2018) explored the interaction between macroeconomic elements, firm traits and financial performance of listed non-financial firms in Nigeria. The model reveals that a significant connection exists between firm traits and the quality of financial reporting.

Firm Traits

Charles et al., (2018) stated that firm traits are elements mostly at the mercy of management. The firms traits include firm age, liquidity, sales growth, firm size, institutional shareholding, board composition and leverage. Fathi, (2013) opined that variables explanatory disclosure quality about firm traits are in three categories such as; structure, market and performance variables. As a result of the preceding studies, accessibility of data and its applicability to the socio-economic environment of Nigeria, two independent variables of the firm are chosen as proxies for firm structural traits; these variables are: firm size and leverage.

Firm Size

In empirical corporate finance works, firm size has been controlling and extensively accepted among the most notable variables (Kioko, 2013). However, studies rendered a varied outcome on the influence of firm size while some attest, other find varied or no influence at all. It was showed that the association linking financial performance and firm size is negatively mediated by indebtedness (Lopez-Valeiras et al., 2011).

Ishak et al., (2018) asserted large firms to be more probably encounter higher agency difficulties. The operations of a larger firm would be tough to run mostly when a line of business is widened. A positive relationship is revealed by firm size with actual earnings manipulation. The implication of the outcome shows the existence of earnings manipulation in large firms. This may result from a large size of transactions in conjunction with some problems control by large firms, which avails the manager the opportunity to influence the transaction to their advantages.

Leverage

The ratio of debt to equity in the capital structure of a firm debt funds is referred to as leverage (Omondi & Muturi, 2013). The business and financial risk of a firm are measured by leverage ratio. According to Ishak et al., (2018), highly geared firms are more bothered with debt covenant because of their reliability on debt to fund new businesses that are riskier. An extensive debt rate would terrify shareholders from insolvency risk. It is evident from studies that firms that are highly geared are prone to take part in earnings management to meet debt covenant. Taken cognizance of extensive and expansion in insolvency risk, the position of debt will notify leaders of jeopardizing their remuneration and other benefits which in succession makes leaders to embrace efficient management strategies as well as conformity with a good governance procedure.

Firm Age

(Paramitha and Rohman, 2020) stated that firm age can be ascertained by considering its starting point. It refers to the span of life of a firm from the time it was found till as long as the firm exists. The firm that has been in existence for a longer period will be well known and have a vast experience as regards the sector it belongs. Firm age depicts the age of the firm at the point of analysis (Yameen et al., 2019).

EMPIRICAL REVIEW

Firm Size and Quality of Financial Reporting

Ishak et al., (2018) carried out an examination on firm traits and the quality of financial reporting: the moderating role of Malaysian corporate governance index. Earnings management was used as a replacement for quality of financial reporting. The data used were secondary sourced from Thompson Database; their outcome revealed that relationship exists only among audited firms by Big 4 and earnings management. As regards the study's contribution, the importance lies on the development of Malaysia Capital Market and also aid investors to appreciate better how corporate governance apparatus have effect on the quality of financial reporting across firms.

Al and Ahmed, (2012) studied on the disclosure of financial reporting by aiming on the firm structure as a determinant of Bangladesh listed non-financial firms; the outcome showed an association that is positively strong between standard of financial reporting and firm structure of listed non-financial firms in Bangladesh. Also, a positive significant connection was established between the firm size and quality of financial reporting; also, a relationship that is significant between quality of transparency in the annual reports.
Agyei-Mensah, (2014) in their study, standard of financial reporting before and after IFRS adoption in Ghana was examined; including the influence of firm specified traits. These specified variables are; audit firm size, liquidity, a debt equity ratio, profitability, and firm size. The results of the findings expressed in multiple regression analysis revealed an association at a statistically significant level between firm size and quality of financial information disclosed. The users are guaranteed of helpful information for making a financial decision based on the enhancement in the standard of the financial reports following the adoption of IFRS.

Asegdew, (2016) assessed the factors of quality of financial reporting in large non-financial share firms in Addis Ababa. In this study, documented analysis of audited financial statements was used, including an extensive interview with the representatives of non-financial firms. The outcome of the analysis by panel least square regression revealed that: share dispersion, type of auditor and firm profitability have a positively and statistically significant connection with the standard of financial reporting of manufacturing share firms. Nevertheless, a negative and statistically significant connection exists between firm size as well as the standard of financial reporting of manufacturing share firms.

Moreover, Wang et al., (2015) considered the association between the quality of financial reporting and investment efficiency in order to analyze the association effect between financial reporting and free cash flow on investment efficiency. The findings of the study revealed that quality of financial reporting is more strongly connected with over investment for firms with large free cash flow, which indicates that quality of financial reporting can decrease the information asymmetry arising from agency conflicts between investors and managers.

Okunbor and Dabor, (2018) examined the association between the firm's market structure and quality of financial reporting of listed firms in Nigeria. The effect of Ordinary Least Square (OLS) regression with fixed effects of market variables aided by factor indices revealed that, the market structure of the firm had significant influence on quality of financial reporting.

Leverage and Quality of Financial Reporting

Tonye and Seth Sokiri, (2020) assessed the impact of financial leverage on quality of financial reporting of listed non-financial firms in Nigeria. The analyses were done by ordinary least square method. The outcome showed that financial leverage had the connection that is insignificantly positive with quality of financial reporting of listed non-financial firms in Nigeria. Bassiouny, (2016) explored the influence of firm traits on quality of financial reporting of listed non-financial firms in Egypt. The study made use of random effect generalized least square regression model with the aid of STATA program. The outcome showed that financial leverage has a connection that is significantly positive with quality of financial reporting. Rusdiyanto and Narsa, (2020) examined the effect of leverage, firm size and return on asset of quality of financial reporting of Indonesian listed firms. The data was sourced from financial report of listed telecommunication firms on Indonesia Stock Exchange between 2014 and 2018. The outcome revealed that leverage affects earnings management (the quality of financial reporting) positively (negatively) and significantly.

Egbunike and Okerekeoti, (2018) explored the interaction between macroeconomic elements, firm traits and financial performance of listed non-financial firms in Nigeria. Also, the effect of the gross domestic product (GDP) growth rate, exchange rate, interest rate and inflation rate were investigated, while the firm traits include; liquidity, leverage and firm size. The financial performance which is the dependent variable is measured as return on assets (ROA). The study revealed that, exchange and interest rates have no effect significantly but the GDP growth rate on ROA and inflation rate have a significant effect. Also, the firm traits revealed liquidity, leverage and firm size to be significant.
Hassan and Bello, (2013) explored firm's traits from a viewpoint of performance,

monitoring and structure factors and the quality of financial reporting measured by the modified model of Dechow & Dichev, (2002) of listed non-financial firms in Nigeria, The results showed that larger and more leveraged firms in Nigerian non-financial sector are less likely to manage earnings and an increase in sales as well as institutional investors serve as a monitoring tool of stopping managers from opportunistic conduct in managing earnings.

Firm Age and Quality of Financial Reporting

Kartiningsih and Daryanto, (2020) examined the effect of firm traits to profitability of food and beverage firms listed in Indonesia Stock Exchange. They employed multiple linear regression analysis to check the correlation and effect of independent and dependent variable. The outcomes showed that firm age, leverage and liquidity have a positive and significant effect on the profitability.

Benjamin and Mailafia, (2016) studied the effect of firm traits on standard of financial reporting of listed petroleum firms in Nigeria. They employed secondary source for data gathering and used the Ordinary Least Square regression technique for analysis. The outcome showed that, firm age affects standard of financial reporting of listed petroleum firms in Nigeria positively and significantly.

Farouk et al., (2019) assessed the influence of traits of firm on quality of financial reporting of listed Industrial Goods firms in Nigeria. The study employed correlation design using a panel balanced data of sampled 11 firms for the period of 2012-2018. The outcome stated that, firm age influences quality of financial reporting of listed Industrial Goods firms in Nigeria negatively and significantly.

THEORETICAL REVIEW

Agency Theory

Jensen and Meckling, (1976), posited agency theory on which this study was built. The theory is regarded as an agreement involving shareholders and external auditor to direct the activity of management. Management’s roles to be carried out are assigned to them by shareholders. The assigned role to be done mainly entails, running the firm on behalf of the shareholder in order to fulfill their goals and objectives. Agency theory lies on the fact that the managers are normally inspired by their benefit and labour to maneuver their gains instead of considering shareholders’ benefit and boosting shareholders’ worth as long as, shareholders act reasonably in boosting their utility ((Toukabri et al., 2014).

METHODOLOGY

This study adopted the longitudinal (panel) research design. The population of listed non-financial firms in the Nigerian Stock Exchange as of 31st December 2020 was 112. The selection of 72 listed non-financial firms was through purposive sampling techniques as a result of availability of their annual financial reports. Data on quality of financial reporting, leverage, firm size, and age of firms were drawn from annual statements of the listed non-financial firms between 2012 and 2020. Descriptive statistics, panel fixed effect and panel regression techniques were used to establish the link between the identified independent variables and quality of financial reporting.
Quality of financial reporting was measured using modified (Dechow & Dichev, 2002) model.

$$\Delta WCit = \lambda 0 + \lambda 1CFOit - 1 + \lambda 2CFOit + \lambda 3CFOit + 1 + \lambda 4\Delta REVit + \lambda 5PPEit + \varepsilon$$

Where; ΔWC= change in working capital, CFO=Cash Flow from Operations, ΔREV=change in revenue, PPE= plant, property and equipment
Quality of financial reporting in the regression model above set out for the study was represented by the residuals for the modified Dechow & Dichev, (2002) model after inserting the sampled data. Furthermore, the accrual quality was decided by the residuals; the smaller the residuals, the higher the quality of accruals, vice versa, (McNichols, 2002). The summary explanation of the variables employed in the work is outlined in Table 1.

Table1: Measurement of variable

Dependent variable	**Variable Label**	**Measurement**	**Source**	**Expected Sign**
Quality of Financial Reporting	QFR	Discretionary Accrual (DAC)	Soyemi & Olawale, (2019)	
Independent Variables				
Firm size	FS	Natural log of total assets	Hamidzadeh & Zeinali, (2015)	±
Leverage	LEV	Ratio of total debt to total asset	Ishak *et al.,* (2018)	±
Firm age	FIRA	The number of years since the firm has been listed on the Stock Exchange	(Olowokure et al., (2015)	+

Source: Authors' compilation (2021)

Model specification

The model specification for this study was grounded on the lessons learned from the appraisal of theoretical literature as well as empirical literature on the link between firm traits as well as the quality of financial reporting. To empirically ascertain how firm traits influence the quality of financial reporting of listed non financial firms in Nigeria, a model put forward by Soyemi & Olawale, (2019) was used as specified in functional and stochastic forms.

$$Qfr = f(Fs, Lev, Fira) \qquad (1)$$

$$Qfr_{it} = \lambda_0 + \lambda_1 Fsz_{it} + \lambda_2 Lev_{it} + \lambda_3 Fira_{it} + \varepsilon_{it} \qquad (2)$$

Where:

Qfr = Quality of financial reporting represent DAC;

Fsz = Firm size;

Lev = Leverage;

Fira = Firm age;

λ 0 = Constant term;

λ 1,..λ3 = Regression Coefficients;

ε = Error term;

i = Firms;

t = Time

RESULTS AND DISCUSSIONS

Descriptive Analysis Results

The recap statistics of variables utilized in this work are outlined in Table 2. The estimated average discretionary accrual for the sampled firms within the sampled period is 0.082 including a minimum as well as a maximum estimated of 0 and 1.017 respectively. The estimated average financial leverage is 64.898 percent with a minimum of 4.285 and a maximum of 395.45 percent. The estimated average firm size is 7.11 including a minimum of 5.239 as well as a maximum of 9.241. Also, the average of the sampled firm is 26.866 years with a maximum age of 55 years and minimum age of 2 years.

Table 2: Descriptive Statistics

Variables	Obs.	Mean	Std. Dev.	Min.	Max.
DAC	648	0.0820	0.106	0.000	1.017
LEV	648	64.898	37.042	4.285	395.450
FSIZ	648	7.1110	0.839	5.239	9.241
FIRA	648	26.866	13.482	2.000	55.000

Source: Authors' Compilation, 2021

Matrix of Correlations Results

The correlation coefficients outcomes among the variables are outlined in Table 3. From this result, the estimated correlation coefficient of 0.404 shows that financial leverage is positively connected with the discretionary accrual. The estimated correlation coefficient of -0.075 implies that firm size has an inverse relationship with discretionary accrual and by extension indicates a relationship that is positive between quality of financial reporting and firm size.

Table 3: Matrix of correlations

Variables	(1)	(2)	(3)	(4)
(1) DAC	1.000			
(2) LEV	0.404	1.000		
(3) FSIZ	-0.075	-0.060	1.000	
(4) FIRA	-0.055	-0.007	0.100	1.000

Source: Author's Compilation, 2021

Variance Inflation Factor Results

The first diagnostic test conducted is the test of multicollinearity using variance inflation factors. The results of the variance inflation elements are outlined in Table4. The outcomes reveal that firm size has 1.014 VIF, firm age has 1.01 VIF, and leverage has 1.004 VIF. Because all the independent variables have VIF that is far below the threshold of 10, then the estimated results are free of multicollinearity.

Table 4: Variance Inflation Factor Results

	VIF	1/VIF
FSIZ	1.014	.987
FIRA	1.010	.990
LEV	1.004	.996
Mean VIF	1.009	

Source: Authors' Compilation, 2021

Regression Diagnostic Tests Results

The presence of serial correlation is also examined using Wooldridge serial correlation test in panel data. The outcomes of the test with 0.258 F value and 0.6129 p value denote that the null hypothesis cannot be rejected at any conventional level of significance. Thus, the model is free of serial correlation. The estimate of 220.52 Breusch-Pagan Chi square value with 0.000 p value thus, significant at 1 percent level specify that the heteroscedasticity problem is visible.

However, the study conducted an examination to choose among the three alternative panel regression techniques namely; pooled OLS, fixed effect and random effect. F test is conducted to test for the presence of firm effects. The null hypothesis on which the test is based is that firm effect does not exist. The outcome of the examination presented in Table 5 with F value of 4.33 and p value of 0.000 indicates the null hypothesis is rejected at 5 percent level of significance. Thus, there is firm effect and using pooled OLS would produce inefficient results. The implication of the result is that the appropriate method is between fixed and random effect model. In order to select the most efficient between a fixed and a random effect model, the study conducted Hausman test which is based on the null hypothesis that the differences in coefficient are not systematic (fixed) and the outcomes are presented in Table 5.

Table 5: Regression Diagnostic Test Results

Test	Test Types	Values	P values	Conclusions
Firm Effects	F-Test	4.33	0.000***	Presence of firm Effects
Systematic Difference	Hausman	12.95	0.0048***	Fixed affect is better
Autocorrelation	Wooldridge Test	0.258	0.6129	No serial correlation
Heteroskedastic	Breusch-Pagan	220.52	0.0000***	Presence of heteroscedasticity

Source: STATA result extract, 2021.

Note: *,*** and * significant at 1%, 5% and 10% respectively**

Estimated Panel Regression Results

Since the result reveals a Hausman chi-square value of 12.95 alongside p values of 0.0048, this implies that fixed effect panel regression is preferred for this study as outlined in column 2 of Table 6. The results in Table 6 are those obtained with pooled OLS presented in column 1, the fixed effect which is presented in column 2 and that of a random effect which is presented in column 3. In line with the outcome of the Hausman specification test, the focus is on the results of the fixed effect panel regression results. In addition, given the results of the pre-estimation diagnostic tests which suggest no serial correlation but presence heteroscedasticity, the outcome of the panel regression in Table 5 are obtained with robust standard error. From the outcomes of the fixed effect panel regression in Table 6, the estimated coefficient of 0.000582 reveals that leverage had a significant positive influence on discretionary accrual as confirmed by 0.000 corresponding p value. The inference of the results is that the connection between leverage as well as the quality of financial reporting of listed non-financial firms.

Table 6: Estimated Panel Regression Results

VARIABLES	POLS(1)	Fixed Effect(2)	Random Effect(3)
LEV	0.00115***	0.000582***	0.000870***
	(0.000)	(0.000)	(0.000)
FSIZ	-0.00587	-0.0539*	-0.00864
	(0.202)	(0.0503)	(0.266)
FIRA	-0.000377	0.00146	-0.000346
	(0.185)	(0.334)	(0.466)
Constant	0.0595*	0.388**	0.0964*
	(0.0816)	(0.0318)	(0.0873)
Observations	648	648	648
R-squared	0.168	0.459	0.368
Number of PID	72	72	72

pval in parentheses

*** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$

Source: Authors' Compilation 2021

In particular, the study found that higher leverage encourages earning manipulation by the management which translates to lower the quality of financial reporting. These results align with the apriori expectation of the study as well as the proposition of the debt covenant hypothesis within the framework of the positive accounting theory that management engaged in earnings manipulation in order to show that the firm is capable of fulfilling the debt obligation to the firm's creditor. The finding here is in agreement with previous empirical literatures that have recorded significant positive impact of leverage on the quality of financial reporting (Bassiouny, 2016; Rusdiyanto & Narsa, 2020; Tonye & Seth Sokiri, 2020).

Similarly, the outcomes of the panel fixed effect in column 2 with -0.0539 estimated coefficient and 0.0503 p value for firm size reveals that the size of the firm has a negative significant effect on the discretionary accrual of listed firms in question. The implication of the outcomes is that the firms influence the quality of financial reporting of listed firms in question negatively and significantly; larger firms produce better quality of financial report. The results found here are in accordance alongside the outcome of Charles et al., (2018) that detailed a positive significant influence of firm size on financial reporting in the study of Nigeria consumable goods firms.

However, considering the control variable of the study, 0.00146 estimated coefficients with 0.334 corresponding p value reveals that the age of the firm has no significant influence on the discretionary accrual. This indicates that firm age does not affect the quality of financial reporting of listed non-financial firms in Nigeria.

CONCLUSION AND RECOMMENDATIONS

The study explored the influence of firm structural traits: leverage and firm size on the quality of financial reporting of listed non-financial firms in Nigeria. The work centered on the data gathered from 72 sampled listed firms on the Nigeria Stock Exchange which was analyzed using fixed effect panel regression based on the outcomes of different specification tests conducted in the study. The quality of financial reporting was proxy with discretionary accrual; measured using Dechow & Dichev, (2002) accrual.

The findings from the fixed effect panel regression revealed that leverage had a significant positive influence on quality of financial reporting of listed non-financial firms in Nigeria.

On the contrary, the results of the fixed effect panel regression indicate that firm size negatively and significantly influences the quality of financial reporting of listed non-financial firms in Nigeria. The findings affirm the proposition of financial distress theory which posits that firm with higher debt ratio are prone to engage in earning management in order to give the creditors an impression that the firm is solvent and can repay the debt. Hence, the study recommends that leverage should be made optimal by firms so as to limit their exposure pressure of having to engage in earning management while trying to assure creditors of the firm’s ability to repay loans.

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