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Original Research Article

IFRS and Timely Loss Recognition of Listed Deposit Money Banks: A Nigerian Experience

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Abstract
This paper investigates the effect of International Financial Reporting Standards (IFRS) adoption on timely loss recognition of listed Deposit Money Banks (DMBs) in Nigeria using ex-post facto research design. A sample of 12 listed DMBs was used. The data on timely loss recognition was extracted from the audited financial statements of the sampled banks for the period under investigation (2006 to 2020) to cover the pre and post IFRS adoption period. The findings revealed a decline in timely loss recognition. The implication is that the adoption of IFRS has not improved accounting information quality as measured by timely recognition of losses.

Keywords: Timely loss recognition, accounting information quality, IFRS, Nigeria.

JEL Classification Code: G20

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INTRODUCTION

IFRS are principle-based standards issued by the International Accounting Standards Board (IASB), an independent organisation registered in the United States of America but based in London, United Kingdom. They pronounced financial reporting standards that ideally would apply equally to financial reporting by public interest entities worldwide. Before the IFRS adoption era, most countries had their own local standards with their regulatory bodies responsible for developing and issuance of the local standards even if some of them align with the IAS. In this vein and in the Nigerian context, the Nigerian Accounting Standards Board (NASB) was responsible for developing and issuing standards known as Statements of Accounting Standards (SAS) and in the new dispensation, the body was renamed Financial Reporting Council (FRC) of Nigeria as the regulatory body overseeing the adoption and implementation of IFRS.

Timely loss recognition is an important measure for evaluating accounting information quality. It is correlated with the conservative and the prudence principles of accounting (Dobre, Brad & Ciobanis, 2015). Tanko (2012) defines it as an organisation's ability to recognise losses as they occur by not indulging in activities that defer losses to other periods. When assuming clean surplus accounting, all changes reported in the statement of financial position are also included in the earnings. So, when gains and losses are timely integrated in the earnings, financial statement and earnings truly reflect more the underlying economics and this improves accounting quality. In this line of thought, the recognition of gains and losses are of equal importance. However, the literature on this topic focusses on the timely recognition of losses (Christensen, Lee & Walker, 2008; Chen, Tang, Jiang & Lin 2008; Paananen, 2008).

The explanation is that managers have incentives to report gains promptly because it can attract bonuses, the chance of violating debt covenants and the costs of debt agreements. The recognition of losses, however, is less favorable for the same reasons: it lowers the bonus, increases the chance of violating debt covenants and increases cost of debt agreements. The management thus has incentives to defer losses to future periods and at the same time has incentives to incorporate gains or good news in the current period. The second reason for using recognition of loss instead of gain recognition is that accounting standards like IFRS suffer from conditional conservatism. The standards are biased towards the recognition of unrealised losses because of the prudence principle. This principle means that accountants want to anticipate losses by incorporating them in the financial statements when it is probable that they occur while gains are not anticipated and are only incorporated in the financial statement when they in fact occur.

Timely loss recognition has different outcomes depending on the company's situation for different stakeholders. Following different outcomes as stated by Brenet (2012); for lenders: they focused on timely accounting recognition of economic losses. Because of lenders' asymmetric payoff from firms' net assets, lenders are concerned with the lower bound of a borrower's net asset value. Timely loss recognition ensures, however, that expected losses are reflected in the financial statements earlier and that the borrowers' true net asset value is not overstated. This lower bound is informative to the lenders in making lending decisions and in specifying

financial covenants. For bond holders and shareholders, timely loss recognition plays a significant role in mitigating conflicts over dividend policy and in reducing firms' borrowing costs. Given these costs, firms face a trade-off when choosing how timely to recognise economic losses.

Timely loss recognition is relevant to creditors as it provides a lower bound measure of earnings. It provides investors with relevant feedback value, and it increases the quality of other information, since this accounting information can be verified with timely loss recognition amounts (Tanko, 2012; Musa, 2015; Chua, Cheong & Gould, 2012). Furthermore, since it constrains management opportunism, timely loss recognition amounts are more reliable. So, the timelier losses are recognised the, the better the quality of accounting information is.

It is expected that firms with a higher quality of accounting information will exhibit a greater frequency of large losses. This characteristic is closely related to earnings smoothing in that if earnings are smoothed, large losses would be rare. Ball, Robin, and Wu (2003) assert that timely loss recognition increases the economic efficiency of firms' contracting with both debt holders and management; timely loss recognition decreases the likelihood of managers making ex ante negative NPV decisions, such as ''trophy'' investments or acquisitions, whose cash flow consequences extend beyond their tenure.

Evidence on the effect of IFRS adoption on timely loss recognition is also mixed. Some studies find that companies recognize losses timely post IFRS adoption (Barth, Landsman & Lang, 2008; Ames, 2009.) while other findings suggest that losses are not recognized timely post IFRS adoption (Dobre, Brad & Ciobanis, 2015; Paglietti, 2009, Umobong & Akani, 2015) there by creating a gap to be filled by this study in the midst of conflicting findings.

LITERATURE REVIEW

Literature on timely loss recognition also revealed conflicting results. Some of the studies confirmed more timely loss recognition indicating an increase in accounting information quality. Other studies confirmed less timely loss recognition after the adoption of IFRS. The studies are reviewed below in ascending order.

Ball, Robin, and Wu (2003) explored the effect of standards and incentives on the quality of financial reporting in four East Asian countries (Hong Kong, Malaysia, Singapore, and Thailand) for the period 1984-1996 using 2726 annual earnings announcements. The study used regression analysis and the result showed that financial reporting quality is not higher under code law, with quality operationalized as timely recognition of economic income (particularly losses).

Barth, Landsman, Lang, and Williams (2006) compared measures of accounting quality for firms applying IAS with US firms using timely loss recognition as one of the metrics of accounting information quality. They used regression and correlation analysis for IAS firms from 1994 to 2000 in comparison with US firms from 1995-2002. They found that IAS firms exhibit lower accounting quality relative to US firms in terms of timely loss recognition. The results suggest that firms that apply IAS have lower accounting quality than US firms.

Barth, Landsman, and Lang (2008) evaluated IFRS and accounting information quality by comparing firms using IAS with firms using US-GAAPs from 1995-2002. Timely loss recognition was measured by coefficient of large negative earnings. The result shows a significant positive coefficient on LNEG suggesting that IAS firms recognize large losses more frequently than the non-IAS firms. The implication of this is that the adoption of IFRS failed to improve the quality of accounting information using timely loss recognition.

The study of Paglietti (2009) examined effect of IFRS adoption and accounting information quality of 92 listed Italian companies from 2002-2007. Timely loss recognition as proxy for accounting information quality was measured by focusing on both large negative net income and the asymmetric incorporation of economic gains and losses into the reported income quality using regression analysis and the result showed no significant increase in the recognition of large losses after IFRS adoption.

Iatridis (2010) investigated the effect of IFRS adoption on the quality of accounting information in the UK using data of 241 non-financial firms from 2004-2005. Timely loss recognition was one of the proxies used for quality of financial statement. The result of the logit regression analysis showed more timely recognition of losses after IFRS adoption which implies an increase in accounting information quality. This result may differ with the increase in the number of years.

Lin, Ricardi and Wang (2012) investigated the effect of IFRS adoption on accounting information quality for 63 German High-Tech companies from 2000-2010. Timely loss recognition as one of the metrics of accounting information quality was measured based on the frequency of large negative income using Basu's model. The result showed more timely loss recognition in the pre-adoption period than the posts adoption period indicating that IFRS has led to decrease in accounting information quality in Germany.

Tanko (2012) assessed the effect of compliance with the regulation and provisions of IFRS on the performance of five selected banks quoted on the Nigerian Stock Exchange from 2007-2010. Timely loss recognition was measured by large negative net income (LNEG) using logit regressions. The study found LNEG to be positive which signifies that IFRS firms recognize loss more frequently in the post IFRS adoption period than they did in the pre-adoption period.

Uyar (2013) evaluated the impact of change of accounting standards on accounting information quality using timely loss recognition as a metric to measure accounting information quality. A sample of 208 firms listed on Istanbul Stock Exchange making a total of 1248 firm-year observations was used from 2002-2007. The result of the regression analysis indicated that with the switch to IFRS, companies reported losses more promptly and in a more accurate manner after the adoption of IFRS as compared to the pre-IFRS regime.

Cameran, Campa and Petinicchio (2014) evaluated the effect of IFRS adoption on earnings quality of Italian companies from 2005 – 2008, using a sample of 270 pairs of IFRS and non IFRS adopters and a total of 948 firm-year observations. They used earnings management and timely loss recognition as surrogates for earnings quality

and regression analysis was employed as the techniques for data analysis. The results revealed that IFRS adopters do not show higher earnings quality compared with local GAAP adopters indicating that companies that adopt IFRS exhibit higher levels of abnormal accruals and a decrease in timely loss recognition.

Umobong and Akani (2015) investigated the difference in the quality of accounting information for pre and post IFRS adoption by manufacturing firms in Nigeria over a five-year period (2009-2013) for 11 listed cement and breweries manufacturing companies. The study applied Basu (1997) regression model by regressing earnings on returns. The result showed that timely loss recognition is insignificantly larger in the post-IFRS period compared to the pre-IFRS period, indicating insignificant change in accounting information quality.

Weerathunga (2015) appraised whether the application of IFRS is associated with higher accounting quality for Sri Lankan firms using a sample of 157 firms listed on Colombo Stock Exchange (CSE). The result using regression analysis indicates more timely recognition of losses after the adoption of IFRS which means an increase in accounting information quality.

Nnadi and Omoteso (2015) provided evidence on the effect of regulatory environment on financial reporting quality by comparing the financial reporting quality of Hong Kong firms which are cross listed in mainland China using timely loss recognition as a metric of accounting information quality. The result revealed more timely loss recognition after IFRS adoption which by implication indicates increase in accounting information quality following the adoption of IFRS

Indrawati (2015) evaluated the effect of the implementation of IFRS on accounting information of financial firms listed on Indonesia Stock exchange from 2008-2012 using a sample of 62 companies. Timely loss recognition was measured with large negative net income (LNEG) using logit regression. The result showed an insignificant positive coefficient of LNEG which indicates that the Indonesia firms reported LNEG in the period after the implementation of IFRS more often than the period before implementation.

Dobre, Brad and Ciobanu (2015) evaluated timely loss recognition of the Romanian Listed companies considering the IFRS approach for four-year period (2010-2013) using a sample of eight companies. The study employed logit and panel data analysis; the regression result provides evidence of more timely loss recognition for Romanian listed companies after IFRS adoption. The existence of more TLR in the post IFRS adoption era showed an increase in the accounting information quality of the Romanian listed firms. The study period of four years and eight companies is considered inadequate and there is a need to estimate the effect of IFRS on timely loss recognition using larger sample size and more recent data.

From the literature reviewed above, most of the results suggest that timely recognition of losses insignificant following IFRS adoption than the pre IFRS adoption period. On this premise, the hypothesis for this study is stated below;

There is no significance difference in timely loss recognition before and after the adoption of IFRS in Nigeria.

METHODOLOGY

Timely loss recognition measures the ability of organisations to recognise losses as they occur. Previous studies suggest that firms exhibiting more timely loss recognition should recognise large losses in the period in which they occur rather than deferring them to future periods. The population of this study comprises all the twenty-one (21) Deposit Money Banks listed on Nigerian Exchange group as at 2020 while the sample is restricted to 12 banks from 2006-2020 using purposive sampling method bringing the sample to 180 firm-year observations. The selection was on the premise of the following criteria;

i. The Bank must be listed and remain listed throughout the study period.
ii. The Bank must be a Deposit Money Bank.
iii. The Bank must have data throughout the study period.

Ex-post facto research design was used. The data on timely loss recognition were extracted from the audited financial statements of the sampled banks for the period under investigation while the data on the market value of the banks were extracted from the published daily share prices from the Nigerian Exchange group from 2006 to 2020. The processed data were analysed using Stata version 14.2 and results discussed together to enable test of hypotheses and inferences drawn.

The regression model used in measuring timeliness and conservatism was adopted from Basu (2005) with modification as stated below;

$$NIBE_{it}=\beta_0+\beta_1 IFRS_{it}+\beta_2 NEG_{it}+\beta_3 RET_{it}+\beta_4 IFRS_{it}*RET_{it}+\beta_5 NEG_{it}*RET_{it}+\beta_6 IFRS_{it}*NEG_{i,t}*RET_{it}+ \varepsilon_{it}$$

$NIBE_{it}$ is net income before extraordinary items scaled by market value of equity at the fiscal year-end
IFRS= a dummy variable taking the value 1 for IFRS-adoption period and zero if otherwise
RET_{it} is the stock return for the fiscal year-end of t.
NEG_{it} = 1 if RET < 0, and 0 otherwise.

B_3 and β_5 captures the timelines of gain and losses, respectively. In other words, β_3 measures the sensitivity of earnings to good news, and β_5 reflects the incremental sensitivity of earnings to bad news relative to good news. The interest of this study is in measuring whether the incremental sensitivity of earnings to bad news, relative to good news, changes following IFRS adoption. Accordingly, the study expands the Basu model to allow the slope coefficients to vary over periods and over IFRS. Based on the foregoing this study expects positive and significant coefficients on economic gains and loss (β_4 and β_6). This is consistent with timelier incorporation of bad news than good news, and particularly, loss recognition after the adoption of IFRS, in other words, a positive coefficient on β_6 suggests that there is more timely loss recognition in the post-adoption period while a negative coefficient suggests that there is more timely loss recognition in the pre-adoption period.

ESTIMATION RESULTS

Table 1.0 presents the regression result explaining the effect of mandatory IFRS adoption on timely loss recognition.

Table 1.0

IFRS adoption and Timely Loss Recognition

$NIBE_{i,t} = \beta_0 + \beta_1 IFRS_{i,t} + \beta_2 NEG_{i,t} + \beta_3 RET_{i,t} + \beta_4 IFRS_{i,t}*RET_{i,t} + \beta_5 NEG_{i,t}*RET_{i,t} + \beta_6 IFRS_{i,t}*NEG_{i,t}*RET_{i,t} + \varepsilon_{it}$

NIBE	Coefficients (β)	t	P>t	[95% Conf. Interval]	
Intercept	0.1423	3.64	0.0000	0.0658	0.2189
IFRS	0.0158	0.33	0.7410	-0.0779	0.1094
NEG	-0.0368	-0.77	0.4390	-0.1301	0.0564
RET	-0.0684	-1.61	0.1080	-0.1518	0.1496
IFRS*RET	0.0880	1.59	0.1120	-0.0207	0.1968
NEG*RET	0.3638	3.37	0.0010	0.1525	0.5750
IFRS*NEG*RET	-0.9004	-4.97	0.0000	-1.255	-0.5453
F	10.620				
Prob > F	0.000				
R^2	0.269				
Adjusted R^2	0.244				
N	180				

Source: Researcher's Compilation, 2023.

The dependent variable NIBE is net income before extraordinary items scaled by market value of equity at the fiscal year-end and RET is the stock return for the fiscal year-end of t. NEG equals 1 if RET < 0, and 0 otherwise. B_3 and β_5 captures the timelines of gain and losses, respectively. In other words, β_3 measures the sensitivity of earnings to good news, and β_5 reflects the incremental sensitivity of earnings to bad news relative to good news. The interest of this study is in measuring whether the incremental sensitivity of earnings to bad news, relative to good news, changes following IFRS adoption. Accordingly, the study expands the Basu model to allow the slope coefficients to vary over periods and over IFRS. Based on the foregoing this study expects positive and significant coefficients on economic gains and loss (β_4 and β_6). This is consistent with timelier incorporation of bad news than good news, and particularly, loss recognition after the adoption of IFRS.

Results related to timely loss recognition are presented in Table 1.0. The regression coefficient on IFRS*RET is positive but insignificant *(β=0.08, p=0.112)* suggesting that the incorporation of gains is marginally timelier after the mandatory adoption of IFRS. In other words, there are no changes in the timeliness of gain and loss recognition before and after the mandatory adoption of IFRS by DMBs in Nigeria. For the variable of interest β_6 (IFRS*NEG*RET), a positive coefficient suggests more timely recognition of losses in the pre-IFRS period, however, the result is negative and significant (*β=-0.9,*

p=0.000) suggesting that there is more timely recognition of losses in the pre-IFRS era as compared to the post IFRS period. The p-value of 0.00 for B_6 ($IFRS_{i,t}*NEG_{i,t}*RET_{i,t}$) which is less than 0.05 and this led to the rejection of the null hypothesis that there is no significant difference in timely loss recognition of DMBs in Nigeria before and after IFRS adoption and by implication, the study accepts the alternate hypothesis which means there is a significant difference in TLR of DMBs after the mandatory adoption of IFRS in Nigeria.

CONCLUSION

The result revealed a negative and significant coefficient on the variable of interest used which is an indication of more timely loss recognition in the pre-IFRS adoption period than the post IFRS adoption era. That is a higher degree of conservatism and higher accounting information before the adoption of IFRS than the post-adoption period. This finding is consistent with the studies of Lin, Ricardi and Wang (2012) and Umobong and Akani (2015) but inconsistent with findings of Chua (2012); Iatridis (2010); Tanko (2012); Dimitropoulos, Asteriou, Kousenidis and leventis (2013); Uyar (2013); Nnadi and Omoteso (2015) who found more timely loss recognition in post-IFRS adoption period than the pre-adoption era. The implication is that there is a decrease in accounting information quality following the mandatory adoption of IFRS by DMBs in Nigeria. This result is in line with the studies of Lin, Ricardi and Wang (2012); Chebaane and Othman (2013); Kargin (2013); Umobong and Akani (2015); Weerathunga (2015); Perez, Salas and Saurina (2016) and Ajekwe, Ibiamke and Silas (2017). However, the finding is at variance with the studies of Barth, Landsman, and Lang (2006); Iatrisdis (2010); Gebhardt and Novotny-Farkas (2011); Jeno (2011); Chua (2012); Tanko (2012) Uyar (2013); Bolibok (2014); Uthman and Abdul-Baki (2014); Abba, Alabede, Okwa and Soje (2018).

The significant decrease in TLR after the adoption of IFRS in Nigeria means that the quality of accounting information reduced after the mandatory adoption of IFRS in Nigeria. This is consistent with the studies of Lin, Ricardi and Wang (2012) and Umobong and Akani (2015) but inconsistent with findings of Chua (2012); Iatridis (2010); Tanko (2012); Dimitropoulos, Asteriou, Kousenidis and Leventis (2013); Uyar (2013); Nnadi and Omoteso (2015). The study therefore concludes that the quality of account information reduced following the mandatory adoption of IFRS in Nigeria as measured by timely loss recognition.

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