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FAIR VALUE ACCOUNTING MEASUREMENT AND RELIABILITY OF FINANCIAL STATEMENTS

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ABSTRACT
The use of fair value accounting for estimation in financial statements have raised a lot of debate among the banking and accounting regulators around the world. The recent adoption of this method in Nigeria has called for the need to take proactive move to determine its effect on the Nigerian financial system. This study was carried out to ascertain whether fair value accounting (FVA) provide more useful information to users than the historical cost accounting (HCA); and also determined the impact of FVA on users' investment decision making. The study was conducted on Banks that are quoted in the Nigerian Stock Exchange; where a sample of 10 banks was purposively selected. Data were collected from the bank's annual reports and the Nigerian Stock Exchange Factbook were analysed using the content analysis, descriptive and inferential statistics. The result of the study showed that FVA provide more detailed information compared to when disclosures were done on HCA. It was also discovered that during the pre FVA measurement, Earnings per Share ($t = 2.94$; $p < 0.05$); and Net Asset Value per Share ($t = 3.38$; $p < 0.05$) had significant positive effect on Share price; while Price Earnings ratio ($t = 0.71$; $p > 0.05$) also had a positive effect, but it is not significant. While, Return on Equity ($t = -1.38$; $p > 0.05$) affected Share Price negatively. Post FVA however showed that EPS (5.27; $P < 0.01$) and P_E_RATIO (2.37; $p < 0.05$) have significant positive effect on share price while NAVPS (-0.70; $P > 0.05$) and ROE (-0.86 $P > 0.05$) have negative effects. It is concluded that financial performance indices that are driven by market forces are most significant in determining company's share price; which makes fair value estimations more relevant and reliable in investment decision making.

KEYWORDS: Fair Value Accounting, Historical Cost Accounting, Reliability, Banking Sector, Nigeria.

INTRODUCTION
Since the adoption of fair value measurement in developed countries, debates and arguments have continued to emerge concerning the relevance and authenticity of the measurement method to financial operation. There had even been allegations that the method has contributed to market breakdown in the United States stock market (Wiley 2011; Huang, 2009). It was said that the adoption of fair value may have led to unreliability of financial statements and some other said it encourages management to manipulate assets value and reported earnings which make financial statement unreliable (Mintz, 2008; Watts & Ramanna; 2009).

Some other school of thought however debunk the idea by stating that fair value approach is a better measurement tool than the traditional methods; and that preparation of financial statements is moving towards measurement on time value and present value calculations. Masoud & Daas (2014) also argued that fair value should not be blamed for the economic downturn and financial crisis stating the root of the problem is lying outside financial reporting and that it was bad management that led to the losses, not fair value accounting (Michael, Paul & Eugene, 2008).

The debates about the appropriateness of fair value accounting has led to the publication of several papers and research works by different authors (Wiley, 2011); Ijeoma, 2013; Betakova Hrazdilova-Beckova, & Skoda, 2014; Al-Khadash & Khasawneh, 2014; Enahoro & Jayeoba, 2013; Kumar 2015). The arguments of the authors oppose or affirm the fact that fair value accounting has contributed to the crisis because it provided investors with needed accurate and complete information concerning companies' financial position. Furthermore, they argue that before a financial statement could be reliable they ought to be verifiable and neutral and since fair value is inferred from the market price of a given asset or liability, it fulfils both qualities. In the midst of these arguments, the Nigerian accounting regulatory bodies adopted the use of fair value accounting for financial statement disclosure as a part of continuous effort to harmonization through the adoption of international financial reporting standards (IFRS). If these arguments still exist in the developed countries, there is need to do a proactive investigation on the effect of this estimation method on the reliability of financial statement in caparison to the methods earlier used (historical cost accounting).

Nigeria, in a bid to comply with emerging trends in the global financial system, have adopted FVA measurement for preparation of items in the financial since its transition to adoption of International Financial Reporting Standards in 2012. Considering the peculiarity of Nigeria as a developing country with considerable economic force in Africa, and the existing arguments and debates on the subject matter in the developed countries, there is need to comparatively determine if the measurement method improve the quality(reliability) of information given in the financial statements, and the effect it has on users' investment decision making. The significance of this study to the Nigerian financial system is that it will help stakeholders to know the effect of the application of fair value accounting on the reliability of financial statement; and the study will provide answers to some of the controversial questions raised about the reliability of fair value accounting measurement. Although the fair value accounting measurement is used by all companies in the different sectors in Nigeria; this study is however limited to the banking sector because their market capitalization is significant in the Nigeria Stock Exchange and they have a significant influence in the capital market.

LITERATURE REVIEW

Concept of Fair Value and Historical Cost

IFRS 13 define fair value as the price that would be received to sell an asset or paid to transfer liability in an orderly transaction between market participants at the measurement date. The concept of fair value takes into consideration the market value of assets which is the price at which it will be purchased as at the balance sheet date. This is because, fair value provides current information (market prices) which is determined by the market forces outside the firm which increases the neutrality of the management and decreases its bias, subjectivity and ability to manipulate the financial statements. This assertion was supported by Penman (2007) who stated that the concept of fair value will make the balance sheet to become primary vehicle for conveying information to the shareholders and the profit and loss account will reports the economic income because it recognizes change in value over the period.

The historical cost concept of valuation requires that assets be reported at the amount paid for them when they were purchased originally (historical cost) regardless of increase in the market value. Field (2005) also stated that the amount reported in the financial statement shall be recorded at the amount actually paid for an asset. This therefore means that the historical cost concept does not take into account inflationary factors relating to prices. Penman (2007), says that in historical cost concept, it is the profit and loss account that show the value to shareholders not the balance sheet. The profits report how well the firm has performed in arbitraging prices in input (supplier) markets and outputs (customer) market. Historical cost accounting rests on the assumption that currency in which transaction are recorded remains stable that is the purchasing power remains the same over the periods.

Reliability and Relevance of Fair Value and Historical Cost

The most controversial issue between fair value and historical cost is their relevance and reliability (Christensen & Nikolaev, 2009). After the adoption of IFRS the justification of fair value is not depending any more on its costs and benefits, but on the decrease in the reliability and the increase in managerial discretion. Reliability means that the firm presents faithful and verifiable financial information to the users; Presentation of faithful information requires providing information in which the book value matches the economic value. Verifiability means that the presented information is able to be tested and makes sure that it has the same value of the transaction (Barlev & Haddad, 2003).

Relevance and reliability are the most important attributes of the accounting information, and this is the reason why accounting standards setters require that firms use fair value measurements which provide more recent and relevant information to the investors and creditors than historical cost. These measurements are more useful for users to assess the firm's performance and predict the future view (cash flow, financial position) of the firm. Standards setters do not seem to accept that reliability should outweigh the relevance of financial statements (Christensen & Nikolaev, 2009).

Globalization and the capital market development have shaped the financial statements components and the users' interests. Nowadays, investors concentrate on investments opportunities, performance and future earnings, so cash flow statement has become the most important statement. As a result, the continuous usage of historical cost becomes difficult because its information is not relevant to cash flow statement and it cannot be a base for the prediction of the future cash flow (Barlev & Haddad, 2003).

Historical cost enhances agency costs by hiding the economic value of assets and liabilities and generating hidden-reserves which have been seen by the users as disadvantages of financial reports (Kohler, 1957). Veron (2008) argued that historical cost provides less relevant and comparable information to users. The opponents of historical cost claimed that it distorts the financial statements. Historical cost does not reflect the changes of the market prices and the interest rates. Furthermore, it depends initially on the conservative principle (costs of research and development are rarely capitalized as intangibles and they usually expensed).

Fair Value and Users' Decision Making

Accounting standards setters believe that fair value increases the relevance of financial statements, improves the comparability, transparency and the timeliness of the financial information, which leads to more useful information for users in making their decisions and evaluating equity (Christensen &Nikolaev, 2009). Fair value provides current information (market prices) which is determined by the market forces outside the firm which increases the neutrality of the management and decreases its bias, subjectivity and ability to manipulate the financial statements. It is argued that when a person wants to purchase or sell something the only useful information he needs to know is the amount of money he is going to pay or get, so fair value is considered as useful information for the users (Bassam, 2010).

Shareholders need financial information to assess the equity value and judge the management performance. Therefore, this information should present the current value of the firm. Fair value reflects the up-to-date economic value of the firm which allows shareholders to know how much their firm worth. Managers should use the firm's resources to maximize the shareholders' value and they should choose the best investments for the firm's future and its value. Presenting financial information in fair value helps shareholders to assess the management performance and knowing whether it is doing well or just wasting the firm's resources.

As an investor, in valuing a possible investment opportunity it is important to not only value the company according to the balance sheet but to also consider the income statement and any additional value changes that can arise from the added information gained (Penman, 2009). Fair value provides useful information for the passive investors depending on current market prices and Investors care more about value not historic costs, so financial statements should report fair value. In conclusion, Users of financial statement use fair value accounting information for decision making and this use varies (Kluever, 2012).

Empirical Review

Studies conducted on FVA in different sector confirm that it gives better more useful information to users and enhance reliability (Elfaki & Hamonad, 2015; Ashford, 2011; Enahoro & Jayeoba, 2013; Kumar, 2015; Wiley, 2011; Ijeoma, 2014; and Betakova, Hrazdilora Bockova & Skoda, 2014). Betakova et al (2014) however suggested that both FVA and HCA measurement should be adopted for measurement as a solution to the present debate and argument about the appropriateness of fair value accounting. Shaffer (2011) had a different view that concluded that implementation of fair value accounting may not necessarily provide financial statement users with more transparent and useful reporting and that financial stability may be negatively impacted by FVA due to the connectedness of financial institution markets and broader economy.

Although studies here explored the reliability of FVA, the debates on the subject matter continue to fill the academic and professional space with submissions and suggestions from various authors. Masond & Daas (2014) concluded in his study, after a comprehensive literature review that there is a reason to believe that fair value accounting is more than just a messenger and may have contributed to the acceleration to recent financial crises in a major way. However the submission of the popular study conducted by Laux & Leuz (2010) to find out if fair value accounting contributes to the financial crises; using US banks as focus shedding more light on the reaction of market irrespective of the method of measurement adopted. The study concluded that the claim that FVA exacerbated the crises is largely unfounded. This submission was also supported by studies conducted by (Fahnestock & Bostwick, 2011)

This study was conducted however to perform an indepth analysis of the financial statement of banks quoted on the Nigerian Stock Exchange with focus on some vital parameters that affects users decision making to see if FVA provide more useful information than HCA. The study also explored the effect of FVA measurement on the company share price that is conducted using a pre and post analyses of the adoption of FVA measurement in Nigeria with focus on variable that affect reliability of financial statement that have been picked based on theories and previous studies.

This study is important at this time in the Nigerian economy where government is making effort to be relevant in the world economy by encouraging companies prepare their financial statement according to world standards (IFRS- *FVA*); although this is a laudable development, there is need to investigate the ability of the government to sustain this development considering the peculiarity of the Nigerian economy; because it is not enough to adopt a more sophisticated accounting standard, but the ability to sustain its usage. The banking sector was selected as the focus of this study because of their real time business activities and their high dominance in the Nigerian capital market.

METHODOLOGY

The study covered the financial sector of companies that are quoted in the Nigerian Stock Exchange (NSE); with focus on the banking sector which was selected because the market capitalization of the banks selected makes up about 70% of the sector which makes their influence significant in the market.

Fourteen (14) banks are listed on the banks listed on the NSE as at 2014 and out of these ten (10) banks were purposively selected for this study. Data were collected from secondary sources mainly from financial report of the selected companies which were listed on the Nigeria stock exchange (NSE). This study used annual report of the selected banks and factbook for the period of 2009-2014. The base year was selected in order to do a 3 years pre and 3 years post fair value measurement disclosure in banks' financial statements.

Model Specification

This study made modification to the Ohlson (1995) Model used for value relevance test as adopted in studies conducted by researchers. The model in this study is formulated to determine the effect of fair value accounting information of listed banks in Nigeria on reliability of their financial statement. Share price was used to proxy the reliability of financial statements because this study seeks to take into accounts the development of the shareholders' value through the performance of the banking sector in the capital market in a given year without internal influence from the banks' management; in order to take care of inconsistency in the prices due to market influence the data used are market price not less than three (3) months after the banks' accounting year end. The independent variables were selected in line with previous studies conducted; Earnings per Share was measured on the ratio of profit after tax less Preference dividend and number of ordinary shares outstanding; Net asset value per share as the ratio of net asset value and number of ordinary share; return on equity is however measured as the ratio of profit after tax less Preference dividend and equity capital and price earnings ratio is the ratio of market price per share and earnings per share.

The model of this study is functionally stated as;

$$RF = f\ (EPS, NAVPS, ROE, P/E. \qquad (1)$$

Where: RF= Reliability of Financial Statements
EPS = Earnings per share;
NAVPS = Net asset value per share;
ROE = Return on Equity;
P/E = Price earnings ratio;
β = the coefficients of independent variables;
ε = Statistical error

The econometric equation for the model is specified as

$$RF_{it} = \beta_0 + \beta 1\ EPS_{it} + \beta 2\ NAVPS_{it} + \beta 3 ROE_{it} + \beta 4\ P/E_{it} + e \qquad (2)$$

Where;

$RF = SP$

$EPS = \frac{PAT - PSH}{NoSH}$

$NAVPS = \frac{NAV}{NoSH}$

$ROE = \frac{PAT - PSH}{ECAP}$

$P/E = \frac{MPS}{EPS}$

β0 = Constant parameter/Intercept
β1-β4 = Coefficients of independent variables
e = Error term

The 'apriori expectation' in the model is that all the independent variables will have significant positive effect on share price. The expectation is based on earlier studies and theories reviewed in literatures.

The first objective of this study was achieved using content analysis to analyse some parameters relating to financial statements such as: Reliability of accounting information, Market risk, Assets, Net asset value per share (NAVPS), Non-controlling interest, Users' decision making, disclosure and Manipulation of depreciation and amortization policy. The second objective was achieved using regression analysis.

DATA PRESENTATION AND DISCUSSIONS

Comparison of Disclosure in Fair Value and Historical Cost

From the analysis of parameters analysed in this study as shown in table 1,

Table I: Content Analysis of Pre and Post Fair Value Measurement Period

Subject	Pre-fair value	Post-fair value
Reliability of Accounting Information	Accounting information cannot be verified because most of them are based on estimation.	Accounting information is reliable because they can be verified in the market and shows faithful representation.
Market risk	Financial statement does not disclose market volatility because items are valued and recorded based on management estimation.	Fair value financial statement discloses market volatility because items are valued and recorded based on market price.
Assets	Assets are valued and recorded at historical cost.	Assets are valued and recorded at current market price.
Net asset value per share (NAVPS)	NAVPS is a reflection of book value of net asset per share.	NAVPS is a reflection of market value of net asset per share.
Non-controlling interest	Non-controlling interest is recorded at book value.	IFRS 3 requires Non-controlling interest to be recorded at fair value.
Users' decision making	Accounting information is based on book value. Hence users have to seek current information in the market	Accounting information is as obtainable in the market (based on market price and value) which facilitate decision making.
Disclosure	Historical cost reporting disclosure is relatively limited to accounting policies and methodology used.	Fair value accounting requires a firm to disclose extensive information about the methodology used, the assumption made and risk exposure which serve as guide for users.
Manipulation of depreciation and amortization policy.	It gives room for depreciation and amortization policy manipulation by management.	Fair value eliminates manipulation of depreciation policy by management because assets are valued based on market price.

Source: Author's Compilation (2016)

it is evident that more detailed and useful information is provided for users in the application of fair value accounting than historical cost accounting. This is because the users have ability to verify the position of the accounts in the market and they are aware of the volatility of the market. The findings of this study is in line with the submission of authors such as; Elfaki & Hammad, (2015), Ijeoma, (2014) and Betakova, Hrazdilova-Bockova & Skoda, (2014) among others which stated in these studies, that Fair value accounting enhances the informative power of a financial statement as opposed to historical cost accounting. Fair value accounting requires a firm to disclose extensive information about the methodology used, the assumption made, risk exposure, related sensitivities and other issues that result in a thorough financial statement. As much as the benefits abound, it was however discovered that the more work is done to give these information as the annual reports are much bulkier than before and this will require more cost of production on the company.

Table IIa & IIb shows the stationarity tests of the variables for the pre and post fair value measurement period. All the variables under ADF and PP tests are found to be stationary at levels in the pre FVA period except NAVPS; while in the post FVA all except EPS, NAVPS and SP. As a result, the affected variables have to be differenced once to check their stationary status. At first differencing, the calculated ADF and PP test statistics clearly reject the null hypothesis of unit root for all variables; the ADF and PP tests decisively confirm the stationarity of each variable. Because of the non stationarity of some variables at levels, further check was done using error correction test. This was done to test the long run relationship between the variables. The result of the ECM shows a negative coefficient which indicate that the long run relationship will be adjusted in the long run. Autocorrelation test was also conducted using Durbin-Watson (d*) statistics to check for the presence of autocorrelation. The result shows that d* falls within the range where we do not reject the null hypotheses, and conclude that there is no positive or negative autocorrelation

Table IIa: Stationarity Test of Variables (Pre FVA)

Variables		**Unit Root Tests**		**Conclusion**
		ADF	***PP***	
SP	*Level*	-2.836936***	-2.772119***	I(0)
	First Diff	-	-	
EPS	*Level*	-4.631028*	-4.777020	I(0)
	First Diff	-	-	
NAVPS	*Level*	-2.280309	-2.227117	I(1)
	First Diff	-6.677449*	-6.849002	
ROE	*Level*	-9.607574*	-13.14710*	I(0)
	First Diff	-	-	
P_E_ RATIO	*Level*	-5.240579*	-2.5313155	I(0)
	First Diff	-	-	
Critical Value	***1%***	***-3.679322***	***-3.679322***	
	5%	***-2.967767***	***-2.967767***	
	10%	***-2.622989***	***-2.622989***	

NB: *, ** & *** represent significance at 1%, 5% and 10% level respectively
source: Author's computation with E-view 7.0

Table IIb: Stationarity Test of Variables (Post FVA)

Variables		**Unit Root Tests**		**Conclusion**
		ADF	***PP***	
SP	*Level*	-2.511932	-2.472390	I(I)
	First Diff	-5.749500*	-7.193782*	
EPS	*Level*	-2.473512	-1.961486	I(1)
	First Diff	-4.257258*	-5.996146*	
NAVPS	*Level*	-2.415537	-2.443028	I(1)
	First Diff	-5.060257*	-5.055143*	
ROE	*Level*	-4.158989*	-4.070524*	I(0)
	First Diff	-	-	
P_E_ RATIO	*Level*	-3.605752**	-3.564622***	I(0)
	First Diff	-	-	
Critical Value	***1%***	***-3.679322***	***-3.679322***	
	5%	***-2.967767***	***-2.967767***	
	10%	***-2.622989***	***-2.622989***	

NB: *, ** & *** represent significance at 1%, 5% and 10% level respectively
source: Author's computation with E-view 7.0

Impact of Fair Value Accounting Measurement on Users' Investment Decision Making

In order to objectively determine the impact of FVA measurement on users' investment decisions, regression analysis was done to capture the pre and post FVA effect. This was done to determine if there is any variation that the estimation method has had on the indices usually used by investors to determine company's performance and accounts reliability. The result in table 5 and 6 show the pre and post FVA results. The results indicate that about 64% and 78% of the total systematic variations of the dependent variable have been explained by all the independent variables taken together; this is indicated by the coefficient of determination (R^2) of 0.639 and 0.779 respectively. The 36% and 22% was left unaccounted for by the model, hence captured by the stochastic disturbance term in the model. Thus, the model has a moderate fit of the regression line.

On the basis of the overall statistical significance of the model as indicated by the F-statistic, it was observed that the overall model was statistically significant since the calculated F-value of 11.09 and 22.12 were significant at 1% level of significance respectively. This implies that there is significant linear relationship between the dependent variable (SHARE_PRICE) and the explanatory variables (EPS, NAVPS, ROE, and P_E_RATIO) since at least one of the parameter estimates is significantly different from zero. Furthermore, we can infer that all the variables used in specifying the estimated econometric model are appropriate and acceptable.

The individual statistical significance indicated by the t-ratios shows that during the pre FVA period, NAVPS (3.38) and EPS (2.94) has a significant positive effect on SHARE_PRICE which is in conformity with a similar study conducted by Vjitha & Nimalathasan (2014) considering listed manufacturing companies in Sri Lanka while ROE (-1.38) and P_E_RATIO (0.71) has negative and positive impact respectively, although they are not significant. During the post FVA period however, EPS (5.27) and P_E_RATIO (2.37) has significant impact on share price while NAVPS (-0.70) and ROE (-0.86) has negative impact but are found to be statistically insignificant. From the results obtained in the study, it is obvious that users are more interested in financial performance indices that show the market valuation of companies in taking investments and hence the significance of earnings per share and relationship between market price and earnings per share (P/E ratio). This conforms to the argument of authors on the implementation of fair value measurement and enhancement of reliability of financial statements; Ijeoma (2014), Ashford (2011); Tharmila & Nimalathasan (2013).

Based on the p-value and beta coefficient of earnings per share at 0.000 and 7.82, it show that investors are fully interested in their earnings on each share owned in the company and if items that produces this are not estimated and disclosed at their fair values, it may mislead the users in taking realistic decisions. It is also very interesting to note that during the pre and post FVA period, EPS have continued to be significant to share price and as such, fair value measurement where quotations are based on current information makes the information used by users to determine EPS to be more relevant and reliable.

Table 5: Pre Fair Value Measurement Period

Dependent Variable	Independent Variables	Coefficients	Standard Error	t- Ratio	Probability
SHARE_PRICE		-0.12459	1.774007	-0.070231	0.9446
	EPS	4.014815	1.362259	2.947174**	0.0069
	NAVPS	0.848889	0.252432	3.382846**	0.0025
	ROE	-4.15909	2.997694	-1.387428	0.1776
	P_E_RATIO	-0.02124	0.029693	-0.715191	0.4811

** ** *** represents 10%, 5% and 1% level of Significance respectively*
Source: Author's Computation (2016)
R- Squared = 0.6396
Adjusted R- Squared = 0.5820
F- Statistics = 11.095
Durbin Watson Statistic = 1.855

Table 6: Post Fair Value Measurement Period

Dependent Variable	Independent Variables	Coefficients	Standard Error	t- Ratio	Probability
SHARE_PRICE		-3.94763	2.344078	-1.684086	0.1046
	EPS	7.826486	1.484732	5.270603***	0.0000
	NAVPS	-0.253826	0.36081	-0.703491	0.4893
	ROE	-5.147199	5.870773	-0.867675	0.3890
	P_E_RATIO	0.520569	0.219197	2.37489**	0.0255

** ** *** represents 10%, 5% and 1% level of Significance respectively*
Source: Author's Computation (2016)
R- Squared = 0.7797
Adjusted R- Squared = 0.7445
F- Statistics = 22.126
Durbin Watson Statistic = 2.042

CONCLUSION

It can therefore be concluded that fair value measurement contribute significantly to the reliability of financial statements as the findings of the study indicate that financial performance indices that are driven by market forces are most significant in determining company's share price. It therefore shows that even if financial statements items are disclosed at historical cost or at fair value, users are still very interested in the items that are relevant to the current market situation which gives fair value measurement an edge. Apart from the relevance of information required by users, the study have also shown that fair value accounting provide more detailed information that are contributory to helping users get more relevant and reliable information.

RECOMMENDATIONS

Companies should prioritize the use fair value accounting in order to disclose more useful and relevant information to users of financial statement because they rely on such financial statement for their information need. Although it has been established in this study that it require more cost to meet up with this requirement due to more effort, cost and time needed to make more disclosures, companies should note that the benefit of satisfying the need of its investors (both existing and potential) outweigh the cost.

The business activities of the banking sector is driven towards real time activities because they deal in cash, makes it very paramount that they reveal information that are relevant to the present and reliable to much extent. This assertion have been proven in this study that users of financial statements monitor the activities of the companies using performance indices that are driven by external forces with minimal interest in internal factors. Companies should make effort to meet with this economic drive because if they do not do so, they would be sidelined by the users themselves. It is recommended therefore, that companies adopt measurement methods that would bring about sustainable economic development.

It is evident that today's world economy requires greater use of fair value measurements in financial reporting because it is perceived that fair measurement information is more relevant to investors than historical cost information. It is recommended that conscious effort is made by companies to move with the world economies since this is the intention of the Nigerian government that lead to the adoption of IFRS in preparation of financial statements.

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