THE LIKELIHOOD OF FRAUDULENT FINANCIAL REPORTING AMONG LISTED COMPANIES IN NIGERIA: APPLICATION OF THE FRAUD TRIANGLE THEORY

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by

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Thesis submitted in fulfilment of the requirements for the degree of Doctor of Philosophy

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DEDICATION

Dedicated to

the memory of

Mr. Joseph O. Inekwe

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LIST OF ACRONYMS AND ABBREVIATIONS

AEM	Accrual Earnings Management
BFP	Business Failure Prediction
CBN	Central Bank of Nigeria
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CPA	Certified Public Accountants
CSR	Corporate Social Responsibility
DA	Discretionary Accruals
Etc	Et Cetera
FFR	Fraudulent Financial Reporting
FRC	Financial Reporting Council
FRCN	Financial Reporting Council of Nigeria
FRD	Fraudulent Reporting Detection
FSD	Financial Statement Divergence
FSF	Financial Statement Fraud
FTT	Fraud Triangle Theory
GAAP	Generally Accepted Accounting Principles
GRI	Global Reporting Initiative
IAS	International Accounting Standard
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
IPO	Initial Public Offer

KS	Kolmogorov Smirnov
MAD	Mean Absolute Deviation
MDA	Multivariate Discriminant Analysis
NASB	Nigerian Accounting Standard Board
NDA	Non-Discretionary Accruals
NSE	Nigerian Stock Exchange
REM	Real Earnings Management
ROA	Return on Assets
SEC	Securities and Exchange Commision
SOX	Sarbane Oxley Act

KEBARANGKALIAN PELAPORAN KEWANGAN PALSU DALAM KALANGAN SYARIKAT TERSENARAI DI NIGERIA - PENGAPLIKASIAN TEORI SEGITIGA PENIPUAN

ABSTRAK

Objektif kajian ini adalah untuk mengkaji kemungkinan pelaporan kewangan palsu di kalangan syarikat tersenarai di Nigeria. Menggunakan beberapa proksi teori segitiga penipuan: kecairan, keuntungan, dan tekanan kewangan (elemen tekanan); saiz firma juruaudit, yuran audit, interaksi yuran audit-saiz firma juruaudit, dan tanggungjawab sosial korporat (elemen peluang); pengurusan pendapatan, dan interaksi pengurusan pendapatan-yuran audit (elemen rasionalisasi), kajian ini menguji sama ada pemboleh ubah yang dikenal pasti berkaitan dengan laporan kewangan palsu di Nigeria. Dengan menggunakan set data 516 pemerhatian ke atas syarikat tersenarai bukan kewangan di bursa saham Nigeria dari tahun 2013 hingga 2018, kajian ini menggunakan undang-undang digit pertama Benford untuk mengkategorikan syarikat tersebut menjadi firma penipuan dan bukan penipuan. Dari analisis regresi logistik multivariasi data, kajian mendapati bahawa kecairan dan keuntungan sebagai elemen tekanan secara signifikan berkaitan dengan pelaporan kewangan palsu. Namun, mahupun keuntungan mempunyai hubungan yang negatif, kecairan didapati memberi sokongan untuk hubungan yang positif. Antara proksi elemen peluang, yuran audit didapati mempunyai hubungan negatif yang signifikan dengan laporan kewangan palsu. Berkenaan dengan elemen rasionalisasi, yuran audit menyederhanakan hubungan antara pengurusan pendapatan dan laporan kewangan palsu. Hasil kajian ini mempunyai implikasi pengesanan awal dan pencegahan pelaporan kewangan palsu di Nigeria. Penemuan dalam kajian ini juga dapat mendorong pihak pengawalselia untuk

melihat semula perbezaan yuran audit antara firma audit Besar Empat dan firma audit bukan Besar Empat sebagai usaha untuk meminimumkan kejadian pelaporan kewangan palsu di Nigeria. Akhirnya, hasil dari beberapa ujian tambahan dan pengukuhan yang dilakukan turut menyokong penemuan utama kajian ini.

THE LIKELIHOOD OF FRAUDULENT FINANCIAL REPORTING AMONG LISTED COMPANIES IN NIGERIA: APPLICATION OF THE FRAUD TRIANGLE THEORY

ABSTRACT

The objective of this study is to investigate the likelihood of fraudulent financial reporting among the listed companies in Nigeria. Using several proxies of the fraud triangle theory: liquidity, profitability, and financial distress (pressure elements); auditor firm size, audit fees, auditor firm size-audit fees interaction, and corporate social responsibility (opportunity elements); earnings management, and earnings management-audit fees interaction (rationalisation elements), this study test whether the identified variables are related to fraudulent financial reporting in Nigeria. Using a dataset of 516 firm-year observations of non-financial listed companies on the Nigerian stock exchange from 2013 to 2018, the study uses Benford's law of first digit to categorise the companies into fraudulent and non-fraudulent firms. From the multivariate logistic regression analyses of the data, the study finds that liquidity and profitability as pressure elements are significantly related to fraudulent financial reporting. However, while profitability exerts a negative relationship, liquidity provides support for a positive relationship. Among the proxies of opportunity element, the audit fee has a significant negative relationship with fraudulent financial reporting. In respect of the rationalisation element, the audit fee moderates the relationship between earnings management and fraudulent financial reporting. The results have implications for early detection and prevention of fraudulent financial reporting in Nigeria. The findings in this study could also encourage regulatory authorities to review the audit fee differences between the Big 4 audit firms and the

non-Big 4 audit firms in an effort to minimise the incidence of fraudulent financial reporting in Nigeria. Finally, the outcomes of several additional and robustness tests performed support the primary findings of this study.

CHAPTER 1

INTRODUCTION

1.1 Background of the Study

Given the incessant occurrences of fraud from decades to decades, fraud has become an outstanding issue in the accounting literature and has drawn much attention from regulators, professionals, investors, academic researchers, press and the public (Ines, 2017; Montesdeoca, Medina, & Santana, 2019). Fraud is a generic term, and Donleavy (2016) defines it as the dishonest manipulation of accounts or the improper appropriation of cash or other resources to enrich oneself at the expense of someone else. Thus, fraud is an intentional act of deceit and it comes in different dimensions.

Broadly, fraud is categorised into three, viz - corruption, assets misappropriation, and financial statement fraud (i e, fraudulent financial reporting) (ACFE, 2016). Of these categories, over the years a survey by the Association of Certified fraud Examiners (ACFE) has indicated that although fraudulent financial reporting (FFR) is the least in cases it is the most costly (ACFE, 2016, 2018, 2020). It must however be stressed that the fact that FFR has the least number of cases may not mean that it is the least in occurrences. It could be as a result of the inherent problem of the difficulties in detecting FFR.

FFR or financial statement fraud is defined as an intentional material misrepresentation arising from the failure to report financial information in accordance with generally accepted accounting principles (GAAPs) (The Centre for Audit Quality, 2010). Generally, it is a type of fraud that involves the manipulation of financial statements (Jackson, 2015). Thus, Soltani, Varzeghani, and Ahmadi (2016) have described it as a deliberate falsification of financial statements to provide a false image

of the company. It is also referred to as management fraud because usually, it involves the management. Corporate executives do directly or circuitously manage accounting records and present financial records that are fraudulent through overriding controls or directing personnel to carry out the fraud (Omidi, Min, Moradinaftchali,& Piri, 2019; Jackson, 2015).

FFR has remained a recurring problem in the corporate world and a major aspect of occupational fraud. Even after all the corporate governance reforms in 2002 that have been initiated in the United States and other parts of the world following the Enron saga, FFR is still pervasive. For example, just to mention a few, the case of IBM, in the United States in 2008, Sino Forest Corp, in 2012, Longtop Financial Technologies, in 2011. In India there was the famous Satyam, in 2009, while in China the Real Gold Mining, in 2011, Chinese Forestry, in 2011, Boshiwa International, in 2012. Correspondingly, in Malaysia, there have been several cases, among them are the case of Axis Incorporation Berhad, in 2017, Inix Technologies Berhad, in 2015, Silverbird Group Berhad, in 2016. Nigeria has its fair share of FFR nightmare. For instance, there was the case of Cadbury Nigeria Plc, in 2006, Afribank Plc, in 2009 and, most recently Capital oil Plc, in 2018.

Furthermore, a survey of 34 countries which has been conducted by PricewaterhouseCoopers (PwC) seems to confirm this trend. The survey revealed that in the post-Sarbanes-Oxley era there were located instances of more financial fraud cases amounting to 140 percent increase in the number of financial misreporting (Huang et al., 2017). Also, an analysis of the UK by an accountancy and business advisory firm, BDO LLP (2018) agrees with this trend. It reveals that the number of reported fraud cases in the United Kingdom (UK) has increased exponentially to 577

in 2017 from 212 cases in 2003 – i.e, an increase of 172 percent. Specifically, it was reported that FFR had an increase of 3,918 cases.

Corporate managers have several reasons for manipulating financial statements, hence the increases in the number of cases of financial misreporting. Extant literature documents several reasons why managers may be inclined to manipulate financial statements. The reasons why managers may engage in such actions include meeting or beating earnings expectation of analysts, income smoothing, improvement in compensation or bonus plan, avoidance of debt covenant violation, covering up financial distress (Alhadab, Clacher, & Keasey, 2015; Iatridis & Kadorinis, 2009; Mulford & Comiskey, 2002; Nia, Huang, & Abidin, 2015; Rahman & Sharif, 2013). This behaviour by corporate managers, though intended to put up a good impression has dire consequences on the particular firm that is involved and the capital market in general.

One of such consequences is that FFR present the highest median loss of $954,000 when compared to that of corruption, i.e, $200,000, and assets misappropriation at $100,000 (ACFE, 2020). Also, fine against victim organisations are higher for FFR (19 percent) cases compared to corruption and assets misappropriation with 10 percent and 9 percent cases, respectively. Furthermore, the capital market thrives on trust. FFR leads to the investors' loss of confidence in the firms that engage in such acts and since it is not easily detectable it may lead to a loss of confidence in the capital market as a whole. In addition to the above, FFR could lead to the failure of a firm with all the attendant unemployment and multiplier effects as seen in the case of Enron and many others.

Past studies have investigated FFR, where most of these studies have concentrated on the effect of corporate governance on FFR with an emphasis on

corporate governance mechanisms such as board independence, number of board members, the gender of board members, audit committee effectiveness, and the likes. However, as Razali and Arshad (2014) have pointed out, because most of the studies on the relationship between an effective corporate governance structure and accounting manipulation document have a negative relationship, a significant focus of accounting research has shifted to testing the relationship between and earnings management level and corporate governance. This may explain why most studies in Nigeria tend to focus on earnings management (e.g, Abdullahi & Ibrahim, 2017; Ajekwe & Ibiamke, 2017; Dakata, Kamardin, & Malak, 2017; Okolie, 2014).

Also, most of the studies on FFR were carried out in the Western world and Asia (e.g., (Amara, Ben Amar, & Jarboui, 2013; Huang, Lin, Chiu, & Yen, 2017; Nindito, 2018; Roden, Cox, & Kim, 2016; Skousen, Smith, & Wright, 2009). Expectedly, the variables that have been examined are derived from the context of those countries. However, the fact that the models that have been developed by such studies may not be applicable in the context of another country has long been established in empirical literature. Magnan, Cormier, and Lapointe-Antunes (2011) have stressed this fact when they contend that due to institutional, legal, and ownership structure differences across the globe, the determinants of FFR that have been identified in the United States context may not be applicable in another context.

In addition to the above, the current study differs from past studies in that while most of the previous studies have focused on the prediction of companies that engages in FFR, this thesis is explanatory in focus. Again, the current study covers the period 2012 to 2018, thus utilising a more recent data set compared to existing studies.

Furthermore, there have been few studies on FFR in the context of Nigeria. However, these studies are either limited in terms of coverage or are based on

perception (questionnaire). For instance, Agbaje and Dare (2018) have assessed the impact of profitability on financial statement fraud where they conclude that there is a significant relationship between financial statement fraud and profitability in the Nigerian manufacturing industry. Notably their study is limited in that it has examined only one variable, profitability in relation to FFR and it covers only the manufacturing sector. Tsegba and Upaa (2015), on the other hand, have examined the consequences of financial statement frauds and conclude that in order of severity, loss of jobs, fall in market value, and prosecution of the culprits are the main consequences of financial statement fraud. Apart from the fact that this study is based on the perception of the respondents, it is not geared at understanding the why and how of FFR.

Despite these studies there is a lack of comprehensive study that consider the extent to which pressure, opportunity and rationalisation in corporate settings that are related to FFR in Nigeria. Pressure, opportunity, and rationalisation play an important role in FFR. Examining the relationship between pressure, opportunity, and rationalisation lend itself to the fraud triangle theory (FTT).

The FTT was developed from the seminal work of Donald Cressey in 1953, where, as pioneering seminal work Cressey identified the three necessary preconditions (pressure, opportunity, and rationalisation) for embezzlement to occur, the study is considered as one of the earliest scholarships on fraud. His work which later became known as the fraud triangle theory (FTT) posited that the presence of financial pressure, opportunity and rationalisation is a breeding ground for fraud. In other words, fraudulent activity is more likely to occur in an environment where a person is under pressure, and the person perceives the opportunity for solving the problem of financial pressure through illegal acts that can be concealed, and he or she rationalises his or her offense as something other than a criminal activity. Hence, the

concept of pressure, opportunity, and rationalisation is well defined within the framework of FTT.

Based on the postulation of the FTT, the concept of pressure refers to the motivation for the fraudulent act. As in the individual, the corporate setting has several motivations or incentives to indulge in FFR. This includes but not limited to issues such as meeting or beating expectations, increased pay (bonus-related pay), cover up violation of debt covenant, as well as cover-up misappropriation of assets.

The concept of opportunity, the second element of the FTT refers to the circumstances that are likely to tempt or enable people or firm to act fraudulently or dishonestly (Amara et al., 2013). It is the perceived opportunity of indulging in fraud and not getting caught (Murphy & Dacin, 2011). Various dimension of opportunity can be found in corporate setting but the most acknowledged in accounting literature is the absence and – or a weak internal control system, management override of internal control system, and the collusion to circumvent the internal control system. It is instructive to note that even though the opportunity element and the pressure element are distinct they are closely linked because opportunity can enhance temptation (Gottschalk, 2017).

The third element of the FTT is the concept of rationalisation. This concept has to do with the fraudster providing justification or excuse to make the act look less criminal. As Cressey (1953, p. 129) puts it " although fraudsters recognise their behaviour as criminal from the beginning, they rationalise it in such a way that they conceive of themselves as not entirely responsible for that behaviour". In other words, rationalisation helps the fraudster to deal with the cognitive dissonance that is associated with their behaviour (Akomea-Frimpong & Andoh, 2020). Thus, effective neutralisation or rationalisation reduces the negative effect, encouraging the person to

commit fraud without feeling bad about it (Murphy & Dacin, 2011). Although, rationalisation is difficult to observe (Amara et al., 2013), and has remained a relative enigma (Murphy, 2012), it is a necessary component of the FTT (Amara et al., 2013; Cressey, 1953).

Consistent with the FTT a number of variables are identified in the Nigerian context that could be investigated as possible explanations for FFR. These variables are highlighted hereunder.

Liquidity. Liquidity is fundamental to the long-term survival of a firm. Since liquidity problem affects the firms' profitability (Takon & Atseye, 2015) and other operational aspect of the firm, firms try to keep their liquidity problem out of public knowledge as much as possible. The performance of Nigerian listed firms in terms of cash flow from operations (CFO) to revenue percent, a credible indicator of liquidity (PWC, 2018) is not encouraging. Table 1.1 provides an insight into the liquidity of Nigeria listed non-financial services firms. The table indicates the number of listed firms with negative CFO to revenue percent from 2016 to 2018.

Table 1.1 Nigerian Listed Firms with negative CFO to Revenue percentage

Table 1.1 Nigerian listed Firms with Negative CFO to Revenue Percentage

Year	Number of Firms
2016	19
2017	22
2018	23

Source: Researcher's Compilation from Annual Reports

Table 1.1 shows that liquidity is a problem among listed firms in Nigeria and the problem has been marginally on the increase. This trend is disturbing if this figure is considered in relation to the relatively small number of listed firms on NSE.

Profitability. Profitability is one of the key indices that motivate investors, actual and potential, in maintaining their investment and investing in a particular firm. Cognisance of this, firms try to post a good performance even when the underlying realities suggest otherwise. Extent literature document that declining profitability and-or loss-making firms are associated with FFR rather than profitable firms (Agbaje & Dare, 2018; Dalnial, Kamaluddin, Sanusi, & Khairuddin, 2014; Nia, 2015).

Profit margin, an indication of profitability suggests that listed firms in Nigeria have problem of profitability as shown in Table 1.2.

Table 1.2 Profit Margin of Nigerian listed Non-financial Services Firms

	(In Percentage)		
Sector	2016	2017	2018
Conglomerates	0	-4	6
Construction/Real Estate	-1	1	-5
HealthCare	8	1	1
ICT	-3	-8	13
Natural Resources	-10	-3	1
Oil and Gas	-4	8	5
Services	-2	3	0
Consumer Goods	-1	7	7

Source: Adapted from Research Team (2019)

Table 1.2 shows that most of the firms from the sectors have a negative profit margin in 2016 although there has been an improvement in the trend in 2017 and 2018, which is on the average at a decreasing rate.

Financial distress could also be a possible explanation for FFR. In Nigeria, to avert financial distress there is an increasing trend in restructuring companies that have had close shaves with insolvency (Uwa, 2019), some of such companies are Oando, Etisalat, and Seven-up. Further evidence of financial distress problems among Nigerian firms can be seen in the debt burden that is carried by Assets Management Corporation of Nigeria (AMCON). AMCON was established by the government of

Nigeria in 2010 to purchase toxic assets (loans) from the banks in order to avert imminent collapse of the banking sector. Since its establishment, AMCON has been carrying a burden of delinquent debtors. Table 1.3 captures the trend of debt burden of AMCON from the year 2016 to 2018.

Table 1.3 AMCON Debt Burden

Year	No. of Top debtors	Amount (₦)
2016	100	953.43 billion
2017	350	2.50 trillion
2018	105	906.00 billion

Source: Encomium (2016), Punch Newspaper (2017), Economic Confidential (2018)

Among the debtors that are indicated on Table 1.3 are individuals and companies. Some of the companies are Capital Oil Plc, Arik Airlines, Silverbird Group Platinum Capital, John Holt Plc, Aero Contractors, and Peugeot Automobile Nigeria (PAN).

Auditor firm size. The question of whether the Big 4 provides higher financial reporting quality than the non-Big 4 has remained a debatable issue in Nigeria (Bala, Amran, & Shaari, 2018). However, in Nigeria both the Big 4 audit firms and the non-Big 4 audit firms have attracted criticism from the regulators, media, and the public (Bakre, 2007). Some of the cases that have attracted such criticisms are Cadbury Nigeria Plc and Akintola Williams Deloitte, Afribank Plc and Akintola Williams Deloitte, Ile-Oluji Cocoa Products Ltd and Ijewere Chartered Accountants, Standard Printing and Publishing Company and Adedeji Odubogun Chartered Accountants, African Petroleum Plc and Oni Lasebikan Chartered Accountants, Union Dicon Salt Plc and Oni Lasebikan Chartered Accountants, Stanbic IBTC Holdings Plc and KPMG

(Bakre, 2007; Bala et al., 2018; Daily Independent, 2015; Salaudeen, Ibikunle, & Chima, 2015). Given the above development it will be enlightening to empirically examine the variable, auditor firm size in relation to FFR.

Audit fee. Audit fee is a possible risk factor in financial reporting quality. Hence, there is the existence of guidelines to serve as control for the audit fee that is charged by audit firms; notwithstanding that in this provision there is much latitude for the audit firm in its audit fee pricing. In the Nigerian context this is evidence when there is a change of auditor from the non-Big 4 to the Big 4 or from the Big 4 to the non-Big 4. Table 1.4 summarises some of these developments.

Table 1.4 Audit Fee Changes for Auditor Firm Size

Company	Non-Big 4				Big 4			
	Year	₦m	Year	₦m	Year	₦m	Year	₦m
Academic Press	2015	4.5	2016	4.5	2017	5.5	2018	6.0
Nigeria Enamelware	2017	8.5	2018	5.0	2013	15.0	2014	16.0
Julius Berger	2014	47.3	2015	47.3	2012	30.0	2013	60.0
Presco	2013	12.0	2014	12.0	2015	24.0	2016	31.0
SCOA	2017	6.8	2018	2.0	2014	12.5	2015	14.0

Source: Researcher Compilation from Annual Reports

Table 1.4 shows that the Big 4 commands a higher audit price in Nigeria. Since there are two schools of thought on audit fee, that is, a high audit fee could be a driver of high audit efforts on the one hand or it could compromise the auditor’s independence. This makes audit fee an important consideration in FFR and hence, it’s inclusion as a variable in this study.

In addition, in order to explain the variability in FFR above and beyond the additive effect of the auditor's firm size and audit fee, the interaction term of the two variables was considered. As Jose (2013) has noted, such a consideration provides the important information about how the two independent variables jointly predict the dependent variable. Also, the results of research studies on the effect of the auditor's firm size on FFR is mixed (Semba & Kato, 2019). The introduction of the audit fee as a moderator variable in the current study is geared towards resolving the inconsistencies.

Corporate social responsibility (CSR) is another variable that has been considered in this study. Some companies in Nigeria have made considerable contributions in respect of CSR. For example, between the year 2011 to 2012 these were some of the companies that had contributed: Dangote Groups Nigeria Plc, ₦1.720 billion, Nigeria Breweries Plc, ₦209.3 million Guinness Nigeria Plc, ₦50.8 million (Udeh & Nwadialor, 2014), Nestle Nigeria Plc, ₦8.7 billion (Ekwujuru, 2018), and many others. Notwithstanding the CSR in Nigeria, the above is without stringent regulation and this has remained a façade behind which firms hide their organisations' harmful impact (Zacharias, 2017). Similarly, Okoro and France (2018) document that companies have been accused of using CSR as a tool of cover-up for the negative impact of their activities. Given the lack of regulation and the voluntary nature of CSR in Nigeria, it is considered a risk factor for FFR and thus it is introduced as a predictor variable in this study.

Earnings management, although unobservable this is a risk factor in FFR. Conceptually, earnings management differs from FFR when it is considered on the basis of GAAPs benchmark. However, extant research suggests that earnings management precede FFR. Thus, corporate managers may have the attitude

(rationalisation) of assuming that what they indulge in is earnings management not FFR, and therefore, is not considered bad. This makes earnings management worth considering as a predictor variable in this study.

Furthermore, to examine the possibility that the interaction of earnings management and audit fee affect FFR above and beyond the addictive effect of earnings management and audit fee, the interaction term of earnings management and audit fee is put forward for consideration. A firm may rationalise that paying a higher audit fee may induce an audit firm to turn a blind eye to earnings management practices. The attitude could be a slippery slope to FFR. Also, given the theoretical perception that the apex of earnings management is FFR and the view that the level of audit fee is related to audit quality, the audit fee was introduced as a moderate variable between earnings management – FFR relationship. This could improve our understanding as to whether audit fee could moderate earnings management from developing into FFR or not.

Conclusively, to provide an understanding on the why and how of FFR in Nigeria it is necessary to examine the fraud risk factors that have been identified above. Therefore, in this study the identified variables are tested to ascertain if there is any significant difference between fraudulent companies and non-fraudulent companies in terms of the likelihood of FFR. Thus, the current study is located within the domain of FFR of occupational fraud, to examine the factors that are affecting FFR in Nigeria through the lens of FTT.

1.2 Problem Statement

This study was motivated by a number of factors. First, there is the issue of misstatement and-or restatement of financial statements among Nigerian listed companies. Some of the cases of restatement or misstatement of financial statements

in Nigeria from 2003 to 2018 have been uncovered by the Nigerian Securities and Exchange Commission (SEC) and are revealed in the annual financial reports, which are shown in Table 1.5.

Table 1.5 Cases of Misstatement/Restatement of Financial Statements

Year	No. of Companies	Cumulative Frequency
2003	12	12
2004	21	33
2005	26	59
2006	18	77
2007	37	114
2008	22	136
2009	42	178
2010	23	201
2011	5	206
2012	28	234
2013	29	263
2014	34	297
2015	24	321
2016	35	356
2017	41	397
2018	22	419
Total	419	

Source: Compiled from annual financial statements, and Angahar (2012)

Table 1.5 shows that cases of misstatement of financial statements are a recurring decimal among listed companies in Nigeria. Although the data on Table 1.5 does not give a complete picture of misstatement or restatement among the listed companies due to the unavailability of some companies' financial statement, cumulatively between 2003 to 2018, a total number of 419 cases have been identified. When these number of cases is compared to the numbers of listed companies over the periods, the issue of FFR should be a matter of concern to the operators in the Nigerian capital market. This is important given the fact that the research results suggest that financial statements provide significant insights into the likelihood of fraud occurrence (BenYoussef & Khan, 2017).

Second, is the growing concern over FFR cases in Nigeria. Among the cases that are worth mentioning are Union Dicon Salt Plc in 2002, Cadbury Nigeria Plc in 2006, Afribank Plc in 2009, African Petroleum Plc in 2010, Stanbic IBTC Plc in 2015, Capital Oil Plc in 2017, and Oando Plc in 2018. This should be a cause for concern as accounting fraud or manipulation of financial statements has become an increasingly serious issue over the last two decades leading to the collapse of ostensibly solid firms (Jackson, 2015). This is especially worrisome given the research findings of Dyck, Morse, and Zingales (2017) which have revealed that the unexposed fraud at any point in time is more than two times its visible tip. Having companies failing without any warning signal suggests that unexposed fraud could be higher than the exposed. This development is evidenced in Nigeria when it has been observed that companies in Nigeria suddenly collapse, almost immediately after receiving a clean bill of record from their auditor (Azagaku & Aku, 2018; Okaro & Okafor, 2013).

Third, is the weak regulatory framework in Nigeria. A weak institutional and regulatory system is one of the fundamental issues in Nigeria stride towards sustainable development. Salaudeen et al. (2015, p. 144) captured the development as, "the effectiveness of regulatory bodies in Nigeria in ensuring ethical standards are maintained by corporate managers and professional accountants still remain questionable and in doubt". Historically, regulatory failure has been shown to be the principal cause of the near collapse of the Nigerian capital market (Ahmed & Bello, 2015).

Related to the issue of poor regulatory framework is the high rate of corruption. Poor regulatory system is a contributory factor to the consistent poor rating of Nigeria over time on the corruption perception index by Transparency International. As Adekoya (2011) indicates, companies cannot be disconnected from the corruption that

exists in the society in which they are operating, especially if they are working in an environment of weakened corporate governance as that in Nigeria.

Another issue is the fact that most FFR are detected through the tips from whistle-blowers. A global survey by ACFE (2020) provided evidence that tips were the most common ways occupational frauds were discovered. This trend is not different from what is obtainable in Nigeria. Most FFR detection in Nigeria were through whistle-blowers. This development brings to question the effectiveness of the external audit of financial statements in FFR detection.

Furthermore, over the years NSE has delisted many companies for financial reports filing violations. For instance, between 2016 and 2017, NSE had delisted 22 companies for non-compliance with the obligatory post-quotation standards regarding the filing of financial statements as at when due (News Agency of Nigeria, 2018). Of the 22 companies that were delisted, 20 were from the non-financial sectors. Apart from delisting, fines were imposed on the violating companies. Between 2016 and 2018 huge fines were imposed on companies for failing to submit their quarterly and final financial statements as at when due, as shown in Table 1.2.

Table 1.6 Fines on Companies for Delay in Financial Report Filing

No. of Companies	Amount of Fine (₦' Million)	Year in Default
38	429.5	2018
31	424.9	2017
16	140.0	2016

Source: Compiled from Popoola (2019), Bello (2018), and Egwuatu (2018)

The amounts in Table 1.6 are outrageous considering the low-profit profile of most Nigerian companies. In 2018, for example, Lafarge Africa Plc, Japaul Oil and Maritime Services, and International Breweries, just to mention a few, had reported a

loss of ₦10.3 billion, ₦5.5 billion, and ₦7.1 billion respectively in their third quarter periods (Benson, 2019). For companies that are battling with losses, the fines for failure to file an audited report on time as shown in Table 1.2, further depletes the bottom-line of the company's earnings. The foregoing suggests that the financial report delay could have informational content in relation to FFR. This is especially important given the fact that the delay in the disclosure of financial statements could be symptomatic of FFR which has found support in prior literature. For example, a study by Cao, Chen, and Higgs (2016) have found that late filing firms are associated with lower financial reporting quality when compared to timely filing firms.

Furthermore, Nariman and Sulaiman (2008) documented that in the case involving Chiew Size Sun v. Cast Iron Products Sdn Bhd, it was alleged that the delay in tabling the financial statements was due to no proper accounting records being kept by the companies. Furthermore, they noted that the delay was to cover up the misappropriation of the assets of the company and the illegal removal of the assets of the company by some of the directors. Similarly, the recent case of Oando Plc in Nigeria has evidenced the same fact. On the reason to the delay in releasing its 2014 financial report, a message on the Oando Plc's twitter handle reads "we apologise profusely for the delay in publishing our financials. We thought it better to be thorough than risk inconsistencies" (Kazeem, 2015, para 4). The result of the delay was financial misreporting by the company as hinted earlier.

Also, past studies on FFR have inherent selection bias (Ghafoor, Zainudin, & Mahdzan, 2019). This limitation as observed by Ghafoor et al. (2019) in their study and from similar studies (e.g, Amara et al., 2013; Nindito, 2018; Roden et al., 2016; Skousen et al., 2009; Suyanto, 2009) relates to the use of enforcement action releases or sanctioned vs non-sanctioned firms as fraud proxy. Given this approach, companies

that escaped being sanctioned or companies that are wrongly sanction will be inappropriately categorised which could impact the results. Secondly, research studies using failed or sanctioned firms as proxy for fraud firms are not proactive in focus. Thus, the current study differs from past studies in that fraudulent and non-fraudulent firms were determined using Benford's law. Benford's digital analysis is a powerful fraud detecting technique that specifies the probabilistic distribution of digits for many occurring phenomena for pointing out expected pattern (Varma & Khan, 2012).

Despite the above concerns, research studies on FFR are lacking. As Okaro et al. (2013) point out, formal studies on FFR are few in Nigeria because few cases of such fraud are publicly available. In a similar vein, Herbert, Anyahara, Okoroafor, and Onyilo (2016) have observed that, as it is the case in most Sub-Saharan African countries, many of the corporate governance infractions such as financial statement fraud are not well-documented and published in Nigeria. Thus, this study contributes to bridging the FFR literature gap. Determining the extent of FFR and characterising firms in terms of exposure to fraud risks is important in an effort to understand and minimise FFR in Nigeria. It also contributes to the sparse empirical research studies on FFR in the African Sub-Saharan region.

1.3 Objectives of the Study

The study's main objective is to empirically investigate, through the lens of the fraud triangle theory, the extent to which pressure, opportunity, and rationalisation contribute to the likelihood of FFR among Nigeria listed companies. Specifically, the study seeks:

1. To examine the effect of pressure (corporate liquidity, profitability, and financial distress) on FFR.
2. To examine the effect of opportunity (auditor firm size, audit fee, and CSR) on

FFR

3. To examine the effect of earnings management on FFR.
4. To investigate whether audit fee moderates the relationship between opportunity (auditor firm size) and FFR.
5. To investigate whether audit fee moderates the relationship between rationalisation (earnings management) and FFR.

1.4 Research Questions

To explore the objectives that have been set out in Section 1.3 the following questions are examined for answers:

1. Does pressure (corporate liquidity, profitability, and financial distress) on companies have a significant effect on FFR?
2. Does opportunity (auditor firm size, audit fee, and CSR) have a significant effect on FFR?
3. What is the effect of rationalisation (earnings management) on FFR?
4. Is the association between opportunity (auditor firm size) and FFR moderated by the level of audit fee?
5. Is the relationship between rationalisation (earnings management), and FFR moderated by audit fee?

1.5 Significance of the Study

There are two key ways this study is expected to contribute to the existing literature on FFR. These are theoretical, and practical contributions.

1.5.1 Theoretical Contribution

This study examines the likelihood of FFR in Nigeria. A considerable number of studies on FFR have been conducted using data from the developed world. Studies based on data from Africa are relatively limited compared to those of the developed countries. Given the difference in operating environment and regulations, the current study could provide new insights from the context of Nigeria.

Secondly, the uniqueness of this research over other studies on FFR that have been undertaken through FTT framework is that auditor firm size, audit fee, auditor firm size-audit fee interaction, CSR, and earnings management-audit fee interaction that are considered in this thesis have not been examined in the past by prior research. By examining these unique variables an important contribution is made to the existing literature. Furthermore, although there is extensive research on earnings management, its relation to FFR is underdeveloped. Research on the relationship between earnings management and FFR seems lacking in the context of Africa in general and Nigeria in particular. By investigating whether earnings management relates to FFR among the firms in Nigeria, this thesis provides an additional contribution to the extant literature. Moreover, prior studies provide contradictory evidence on the association between earnings management and FFR (Hasnan, Rahman, & Mahenthiran, 2014; Ines, 2017a; Rahman, Sulaiman, Fadel, & Kazemian, 2016). With the inclusion of audit fee as moderator in the current study this study seeks to contribute to the literature in resolving the inconsistency.

Finally, most past studies on FFR in Nigeria are limited in several ways. Some are too limited in scope. An example is a study on financial statement fraud in Nigeria by Agbaje and Dare (2018) that examines only one predictor variable (profitability) and one sector (manufacturing). Others are limited by methodology. For example,

Tsegba and Upaa (2015) research was based on a questionnaire. This approach could only provide opiniated response which is not very reliable especially on issues as sensitive as FFR. Yet other studies such as Ogoun and Obara (2013), Okaro, Okafor, and Ofoegbu (2013), and Abdullahi, Mansor, and Nuhu (2015) were theoretical in nature. The current study is apparently one of the first comprehensive empirical studies on FFR in Nigeria, and thus adds to the effort to better understand the FFR risk factors in Nigeria.

1.5.2 Practical Contribution

Given that the current research is empirical, current, and more comprehensive compared to prior researches in the context of Nigeria, it is expected to provide a more in-depth explanations and accurate findings. The findings are expected to aid regulatory authorities and other corporate gatekeepers in their effort to curtail FFR in Nigeria. Furthermore, unlike prior studies this study uses Benford's Law in discriminating FFR from non-FFR firms and its integration with the FTT, thus this approach is proactive unlike past studies that are mainly reactive in nature using sanctioned or failed companies. Since proactive detection of FFR results in quick detection which in turn lead to lower losses (ACFE, 2020), the expected findings from this study may contribute to minimising losses arising from FFR.

In the same vein, the expected findings from this study may contribute in enhancing the performance of auditors in the identification of high audit risk factors which could provide the needed input in audit planning. This is especially important considering the prominence that is given to auditing as the anti-fraud mechanism despite its failings in FFR detection.

The findings of this study may provide additional information for the investors in their investment decision making, thereby reducing information asymmetry between the investors and the companies. As the entire data that are used in this study are publicly available, this understanding may provide shareholders and potential investors with the awareness that the published data could be used to gain an insight into the likelihood of FFR by firms in the capital market. This knowledge has the possibility of reducing information asymmetry and enhance the efficiency of the capital market. Besides, investors could also use this understanding to protect themselves from unscrupulous companies

1.6 Scope of the Study

This study investigates the likelihood of FFR in Nigeria using the lens of the fraud triangle theory. The focus of the study is the listed companies in Nigeria, excluding non-listed firms and the listed financial services firms. The financial and insurance companies are excluded because of their operative and regulatory uniqueness. The study examined all the listed non-financial companies that possessed the required data. The period covered is seven years, from 2012 to 2018. The choice of this periods was based on the fact that IFRS was adopted in Nigeria from 2012 and the periods was the most current.

It is recognised that several variables could be used as a proxy for each of the elements of the fraud triangle theory. However, this study restricts the proxy for pressure element to liquidity, profitability, and corporate financial distress. Opportunity element is limited to auditor firm size, audit fee, corporate social responsibility reporting, and the interaction between auditor firm size and audit fee.

The rationalisation element is restricted to earnings management and the interaction between earnings management and audit fee. The study used logistic

multiple regression analysis to analyse the data in assessing the relationship among the variables within the framework of the FTT.

1.7 Definition of Key Terms

Fraudulent Financial Reporting (FFR): "Fraudulent financial reporting is defined as a deliberate falsification of financial statements to provide a false image of the company" (Soltani et al., 2016, p. 191).

Earnings Management: This takes place "when managers use judgment in financial reporting, and in structuring transactions to alter financial reports to both misinform some stakeholders about the underlying overall economic performance of the organisation or to steer contractual outcomes that rely on suggested accounting numbers" (Healy & Wahlen, 1999, p. 6).

Corporate Social Responsibility Disclosure: CSR disclosure is defined as the "process of communicating the social and environmental effects of organisations' economic actions to particular interest groups within society and to society at large" (Nekhili, Nagati, Chtioui, & Rebolledo, 2017, p. 42)

Auditor firm size: The categorisation of accounting firms into two broad divides, the Big 4 and non-Big 4 (big and small) based on their size, reputation and worldwide reach (Stephens, 2017).

Liquidity: This is the ability of a company to meet its near-term obligations when due (Fridson & Alvarez, 2002, p.357).

Profitability: This refers to the company's ability to generate profits as a return on their money invested (Durrah, Aziz, Rahman, Jamil, & Ghafeer, 2016, p. 436).

Financial Distress: Financial distress is a state of affairs wherein a company's financial ability is deteriorating step by step and its incapacity to pay current obligations to creditors (Ufo, 2015, p. 8).

Audit fee: This is the "fee paid for annual audits and reviews of financial statements for the most recent fiscal year" (Yuniarti, 2011, p. 86).

1.8 Thesis Structure

This thesis proposal consists of five chapters. The current chapter presents a background of the study, a brief on the theory underpinning the study (full discussion of the theories is deferred to chapter two), problem statement and the objectives of the study. The chapter also highlights the research questions that drive the study, the expected contributions of the study, and the definition of key terms.

Chapter two provides a summary of the literature concerning the variables that are under consideration in the study. These include the outcome variable (fraudulent financial reporting), the predictor variables (liquidity, profitability, financial distress, auditor firm size, CSR, audit fee, and earnings management), and control variable (firm size, and financial leverage). It presents the underlying theories, the conceptual framework, and hypotheses on which this study is anchored.

Chapter three justifies the research methodology that will be used and discusses the unit of analysis, the population of the study, sampling techniques, and the data collection sources. The chapter also presents the research models, and the operationalisation of the variables that are included in the model. It highlights the statistical analysis and diagnostic tests that will be employed in the study to ensure unbiased parameter estimates and efficient models.

Chapter four highlighted the make-up of the sample size, the descriptive statistics profile, the extent of compliance with logistic regression assumptions. The section also outlined the results from the analysis of the data.

Chapter five presents the discussion of the findings arising from the results of the data analysis in chapter four. It provides a discussion on the contributions of the study, limitations of the study, and recommendations for further research.

CHAPTER 2

LITERATURE REVIEW

2.1 Introduction

This chapter provides a review of relevant literature on FFR and the relevant variables that would constitute the framework of this study. These variables include liquidity, profitability, financial distress, auditor firm size, audit fee, CSR and earnings management. The measurement options of the variables were also highlighted. The chapter also discusses the underlying theories, the research gaps, and empirical studies on FFR based on FTT. The chapter ends with the theoretical framework of the study and the development of hypotheses.

2.2 Overview of Financial Reporting in Nigeria

This section is an overview of the financial reporting in Nigeria. It highlights the principal statutes that are regulating financial reporting in Nigeria, the sanctions, and penalties therein, and an assessment of the level of compliance with the regulations. In other words, the section provides an insight into the state of financial reporting regulations and enforcement in Nigeria.

2.2.1 Financial Reporting Regulations in Nigeria

Financial reporting in Nigeria is governed mainly by three principal statutes. These are the Companies and Allied Matters Act (CAMA), 2020 (repeals 2004 Act), Investment and Securities Act (ISA), 2007, and Financial Reporting Council (FRC), 2011 Act. In addition to these statutes, the Nigerian Code of Corporate Governance 2018 is also