REPORT ON THE OBSERVANCE OF STANDARDS AND CODES (ROSC)
Nigeria

ACCOUNTING AND AUDITING
June 6, 2011

Contents

EXECUTIVE SUMMARY

The Government of Nigeria requested the World Bank in 2010 to conduct a second ROSC A&A review. This ROSC A&A review was conducted to assess the status of implementation of the 2004 ROSC A&A Country Action Plan and identify ways to strengthen the institutional framework underpinning accounting and auditing practices and improve financial reporting in Nigeria. The ROSC exercise was conducted through a participatory process involving key stakeholders and led by the country authorities.

The report finds that there has been limited implementation of the 2004 Country Action Plan and limited improvement in financial reporting practices in Nigeria. Nigerian authorities have successfully implemented only 6 of 14 action plans emanating from the 2004 review leaving significant areas yet to be addressed.

A number of banks exploiting loopholes in Nigerian accounting and auditing standards, weak capacity of the regulatory bodies and weak enforcement, employed creative accounting to boost their balance sheets These weaknesses in financial reporting, auditing and accounting contributed to Nigeria's banking sector crisis. Given the magnitude of the costs of the crisis (between ₦1.5 - ₦2 trillion) government is focused on improving A&A. Since 2009 the CBN, SEC and other bodies have taken considerable steps to improve financial reporting and disclosure standards.

The most important areas for further progress include the adoption of IFRS and promulgation of the Financial Reporting Council (FRC) bill. Government has announced the adoption of IFRS from January 1, 2012, for public listed entities and significant public interest entities. The FRC Bill has recently been passed by the National Assembly and is awaiting the assent of the President. There is greater awareness by investors, directors, managers, and auditors to improve compliance with financial reporting requirements by publicly traded companies largely through the efforts of various regulatory agencies. Monitoring and enforcement mechanisms of accounting and auditing standards and codes have improved (although international audit standards have not been implemented); errant companies and auditors have been sanctioned. The progress is an indication of Government's commitment to improving the quality of financial reporting, a key contributor to enhancing investor confidence and economic growth.

This 2011 ROSC presents policy recommendations that take into account international experience, good practice, and local circumstances. With focus on updating the country's *statutory framework reporting* and *strengthening capacity of accounting and auditing regulatory bodies*, the Companies and Allied Matters Act should be amended. Priority should be given to implementing IFRS, ISA, and ISQC as mandatory requirements. The two *professional accountancy bodies* in Nigeria, ICAN and ANAN, should serve both private and public sectors of the economy and enter into twinning arrangements with the leading IFAC-member bodies.

Students and trainee accountants and auditors should be provided with appropriate training and education in accordance with the International Education Standards (IES) issued by the International Accounting Education Standards Board (IAESB) of IFAC to ensure that they are sufficiently qualified to undertake accounting and auditing activities and assist them in implementing international accounting, auditing and ethics standards and further improving their communication skills, and professional judgment. A summary of the policy recommendations follows in Table 1.

Table 1. Summary of Policy Recommendations						
Actions	***Para No.***	***Responsibility***	***Links with current/ forthcoming projects***	***Implementation Schedule***		
				Short term *(1-2 years)*	***Medium term*** *(3-4 years)*	***Long term*** *(5-7 years)*
1. STATUTORY FRAMEWORK						
(a) Amend the CAMA, 1990 to: • Provide eligibility requirements for the appointment of statutory auditor • Exempt small-size private companies from statutory audit requirements • Set in regulations/guidelines penalties for noncompliance with applicable accounting standards and failure to file financial statements with appropriate authorities at levels that can act as effective deterrents.	57 58 55	Government	None	X		
(b) Prescribe by accounting standards and not law the form and content of financial statements.	56	Government	None	X		
(c) Take immediate steps for enactment of the FRC Bill.	59	Government	None	X		
2. ACCOUNTING AND AUDITING REGULATORY BODY						
(d) Establish and operationalize the Financial Reporting Council immediately after enactment of the FRC Bill, including taking steps to develop FRC institutional capacity.	60	NASB	None	X		

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(e)	The FRC should develop collaborative arrangement with each of the key financial sector regulators – CBN, NDIC, SEC, and NAICOM.	62	FRC	None	X		
(f)	Take practical steps for implementation of the road map to IFRS conversion.	63	Financial regulators forum	None	X		
(g)	Make arrangements for mandating the application of current ISA and ISQC.	64	FRC	None	X		
3. PROFESSIONAL ACCOUNTANCY BODY							
(h)	Develop the accountancy profession to serve both private and public sectors of the economy.	65	ICAN/ANAN	None	X		
(i)	Strengthen institutional capacity of ICAN with the help of a twining partner to enhance the degree of compliance with IFAC statements of membership obligations.	66	ICAN	ICAN, IDF	X	X	
(j)	Build institutional capacity of ANAN with the help of a twining partner to meet the requirements of obtaining IFAC membership.	67	ANAN	None	X	X	
(k)	Pursue vigorously the current ICAN initiative to improve the quality of audit firms to engender quality services.	68	ICAN	None	X	X	

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4. FINANCIAL SECTOR REGULATOR						
(l) Fast-track the current initiative of CBN and NDIC to support the implementation of IFRS in banking sector to meet the mandatory IFRS adoption date of January 1, 2012.	69	CBN & NDIC	None	X		
(m) Develop IFRS technical capacity in SEC and other relevant regulatory bodies.	70	SEC, NSE, CAC, NAICOM, FIRS	None	X		
5. PROFESSIONAL EDUCATION AND TRAINING						
(n) Provide appropriate training and education arrangement in all parts of the country to facilitate IFRS application by corporate entities in Nigeria.	71	NASB, ICAN & ANAN	None	X		
(o) Enhance the academic and professional education and training.	72	NUC, NAA, ICAN & ANAN	None	X	X	

PREFACE

The global financial community considers that the adoption and implementation of internationally recognized standards and codes will provide a framework to strengthen domestic institutions, address potential vulnerabilities, and improve transparency in the economic health of a country. The Reports on Observance of Standards and Codes, Accounting & Auditing Review (ROSC A&A) is 1 of 12 modules developed jointly by the World Bank and IMF after the Asian financial crisis in 1997 as part of a series of measures to strengthen the international financial architecture. These modules were developed in order to assess a country's strengths and weaknesses of actual practices with regards to the various components of financial architecture.[1] The ROSC thus aims to enhance countries resilience to economic shocks and to better support their risk assessment and investment decisions.

The ROSC A&A focuses on the institutional framework regulating the accounting and auditing practices, and the comparability of national accounting and auditing practices with international standards and best practice, using International Financial Reporting Standards (IFRS) and International Standards on Auditing (ISA) as benchmarks. It evaluates the effectiveness of enforcement mechanisms for ensuring compliance with applicable standards and codes. An overview of the ROSC A&A Program, including rationale and detailed methodology, is available at http://www.worldbank.org/ifa/rosc_aa.html.

As a follow-up to the 2004 Nigeria ROSC A&A, the 2011 ROSC presents the status of implementation of the 2004 Country Action Plan and sets out current systemic issues pertaining to the accountancy profession's institutional framework that require strengthening. In addition the report presents policy recommendations for further improving corporate financial reporting regime in Nigeria.

This ROSC was carried out in Nigeria from October 2010 to March 2011 through a participatory process involving in-country stakeholders from the Government, regulatory bodies, accounting and auditing firms, banks, insurance companies, leading corporate business entities, professional accountancy bodies, and academia. It was conducted by a World Bank Team comprising Akinrinmola Oyenuga Akinyele (Senior Financial Management Specialist and Task Team Leader); M. Zubaidur Rahman (Program Manager, OPCFM, and Study Adviser); Philip Segun Olowolaju (Local Consultant); and Nnadi Godson (Local Consultant). The report benefitted immensely from the peer review of Thomas Zimmerman and Szymon Radziszewicz (both Technical Managers, Member Body Department, IFAC); Richard L. Symonds (Consultant, LEGPS, and former Senior Counsel); Volker Treichel (Lead Economist); Ismail Radwan (Lead Private Sector Development Specialist); and Patrick Kabuya (Senior Financial Management Specialist).

[1] The 12 ROSC modules are data transparency, fiscal transparency, monetary and financial policy transparency, banking supervision, securities, insurance, payments systems, anti-money laundering, corporate governance, accounting, auditing, and insolvency and creditor rights.

ABBREVIATIONS AND ACRONYMS

A&A	Accounting and Auditing
ANAN	Association of National Accountants of Nigeria
CAC	Corporate Affairs Commission
CAMA	Companies and Allied Matters Act
CBN	Central Bank of Nigeria
CPD	Continuing professional development
FRC	Financial Reporting Council (proposed)
GDP	Gross domestic product
IAASB	International Auditing and Assurance Standards Board
IAESB	International Accounting Education Standards Board
IAS	International Accounting Standard
IASB	International Accounting Standards Board
ICAN	Institute of Chartered Accountants of Nigeria
IDF	Institutional Development Fund
IES	International Education Standard
IESBA	International Ethics Standards Board for Accountants
IFAC	International Federation of Accountants
IFRS	International Financial Reporting Standard
IMF	International Monetary Fund
IPSAS	International Public Sector Accounting Standards
ISA	International Standard on Auditing
NAA	Nigerian Accounting Association
NAICOM	National Insurance Commission
NASB	Nigeria Accounting Standards Board
NDIC	Nigeria Deposit Insurance Corporation
NSA	Nigeria Standard on Auditing
NSE	Nigeria Stock Exchange
NUC	National Universities Commission
PENCOM	National Pension Commission
ROSC	Report on the Observance of Standards and Codes
SAS	Statement of Accounting Standard (Nigeria)
SEC	Securities and Exchange Commission
SME	Small and medium-size enterprise
SMO	Statement of Membership Obligation (IFAC)

I. BACKGROUND AND COUNTRY CONTEXT

A. Background

1. **This second ROSC A&A review was requested by the Government of Nigeria in 2010 to determine what reforms should be undertaken to further strengthen the accountancy institutional framework that is critical in contributing to the country's economic growth.** This review establishes the extent of implementation of the Country Action Plans prepared following the 2004 ROSC. It also identifies emerging strengths and weaknesses in institutional framework underpinning accounting and auditing practices that influence the quality of financial reporting. It provides policy recommendations to address the identified systemic weaknesses. Ultimately, implementation of the recommendations will improve the corporate financial reporting, which will contribute to enhancement of the quality of Nigeria financial information and business environment and advance governance and financial accountability.

2. **To facilitate collection of data the ROSC A&A Team used a diagnostic template that captures a comprehensive review of institutional framework underpinning accounting and auditing practices in Nigeria.** The data was supplemented by the due diligence exercise involving series of meetings with key stakeholders in capturing primary experiences and other facts on corporate financial reporting practices in Nigeria, including information on the status of implementation of the 2004 Country Action Plan. The review uses International Financial Reporting Standards (IFRS)[2] and International Standards on Auditing (ISA)[3] as benchmarks and draws on international experience and good practice in the field of accounting and audit regulation. An overview of the ROSC A&A and the detailed presentation of methodologies are available on the World Bank website.

B. Country Context

3. **With a population estimated at 150 million (2008 figure), Nigeria is Africa's most populous nation.** Nigeria has one of the fastest growing economies in the world, with a GDP growth rate of about 9 percent in 2008 and 8.3 percent in 2009. Its GDP of US$169 billion (2009) ranks Nigeria's economy the second largest in Africa and 41st in the world, but the country has a nominal per capita GDP of US$1,140 (2009).[4] Nigeria is richly endowed with abundant natural resources, notably oil. A member of the Oil Producing and Exporting Countries (OPEC), Nigeria is the world's 8th largest oil-producer and 6th largest oil exporter. It has the world's 6th largest deposit of gas. The economy remains predominantly rural and agrarian, with agriculture accounting for the largest share of economic output.

4. **Nigeria's financial services sector is dominated by banking.** At end-December 2009, the Nigerian formal financial system comprised the Central Bank of Nigeria (CBN), the Nigerian

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[2] IFRS are issued by the International Accounting Standards Board (IASB), an independent accounting standard-setter based in London, UK. The IASB announced that it would adopt all of the previously issued International Accounting Standards (IAS) issued by the International Accounting Standards Committee (IASC). For simplicity's sake, the term IFRS will refer to both IFRS and IAS in this report.

[3] ISA are issued by the International Auditing and Assurance Standards Board (IAASB) of the International Federation of Accountants (IFAC).

[4] World Development Indicator database (World Bank, 2010).

Deposit Insurance Corporation (NDIC), the Securities and Exchange Commission (SEC), the National Insurance Commission (NAICOM), the National Pension Commission (PENCOM), 24 deposit money banks, 5 development finance institutions, 910 microfinance banks, 5 discount houses, 110 finance companies, 101 primary mortgage institutions, 1,601 bureaux-de-change, 73 insurance companies, 1 Stock Exchange, and 1 Commodity Exchange.[5]

5. **Poor standards of financial reporting contributed to a boom and bust in the financial sector.** Since the completion of the 2004 ROSC A&A, the Central Bank of Nigeria (CBN) raised significantly the minimum capital requirements for a universal banking license from ₦2.5 to ₦25 billion. Small banks exited the market, others merged and all the survivors looked to raise capital on the stock market. In an effort to attain – and in many cases exceed – the CBN's new higher minimum capital requirement, bank managers exploited the lax regulatory climate and provided margin loans to their customers, allowing them to purchase bank shares on credit. Many customers used the margin loans to adopt highly leveraged positions.

6. **By the beginning of 2008, the Nigerian stock market had become hugely overvalued,** with a price earnings ratio of 57 (4^{th} highest in the world), and more than 70 percent of the stock market capitalization was accounted for by banks that had used margin loans to artificially inflate their share prices. This exposed the domestic banking sector directly to risks from the corresponding asset price bubble. As stock prices fell rapidly, customers defaulted on the margin loans which came to account for a large part of the banks' non-performing loan (NPL) portfolio.

7. **The CBN took decisive action to address the situation.** The extent of this exposure was not known in Nigeria until the Central Bank carried out special inspections in the second half of 2009 as the banks had systematically concealed their losses. These special inspections also revealed that banks had sizeable non-performing loan exposures *inter alia* to the downstream oil sector. As a result of the special inspections reported NPLs rose from less than 5% in 2008 to close to 60% by end 2009. Arising therefrom the CBN quickly moved to adopt IFRS for banks and improve bank supervision by moving to consolidated supervision and risk-based supervision.

II. STATUS OF IMPLEMENTATION OF 2004 COUNTRY ACTION PLAN

8. **Nigeria's Country Action Plan, emanating from policy recommendations of the 2004 ROSC A&A, was agreed upon at the stakeholders workshop organized by the Nigerian Accounting Standards Board (NASB) in collaboration with the World Bank on September 13, 2004, in Lagos.** The Plan included 14 actions. To date, 6 of the 14 actions have been successfully implemented, and the Government has taken initial steps toward implementing 4 other actions. These include the adoption of IFRS with effect from January 1, 2012, and the ongoing consideration of the draft FRC Bill by the National Assembly. Table 2 summarizes the current status of progress on the 2004 Country Action Plan.

[5] CBN Annual, Report and Statement of Accounts for the Year ended December 31, 2009.

Table 2: Summary of progress on Country Action Plan resulting from 2004 ROSC A&A

	Country Action Plan	*Led by*	*Status as of February 2011*
1.	Raise awareness (by means of workshops and seminars) of investors, directors, managers, and auditors to improve degree of compliance with financial reporting requirements by public interest entities.	Regulatory bodies; FRC on regular basis once established	Implemented
2.	Improve the statutory framework of accounting and auditing to protect public interest (a) Amend the NASB Act into a Financial Reporting Act. (b) Revise provisions on accounting, auditing, and financial reporting for general purpose financial statements in various laws and regulations to conform to the proposed Financial Reporting Act.	NASB; Regulatory bodies	Partially implemented[/a]
3.	Fully issue the existing IAS/IFRS as Statement of Accounting Standards (SAS)	NASB	Partially implemented[/b]
4.	Fully introduce existing ISA	ICAN	Partially implemented
5.	Nigeria auditing standard-setter issues ISA as soon as they are published by IFAC.	FRC	Partially implemented
6.	Nigeria accounting standard-setter issues SAS on any issue being concluded by IASB almost at the same time.	NASB/FRC	Partially implemented
7.	Introduce simplified financial reporting framework for small and medium-size enterprises.	NASB/FRC	Partially implemented
8.	Professional accountancy bodies should align their CPD requirements with IFAC guidelines.	ICAN and ANAN	Implemented (ICAN)
9.	Business ethics should be taught as a separate subject in undergraduate accounting and business programs.	NAA	Partially implemented
10.	Professional qualifying examinations should include a paper on business ethics.	ICAN	Implemented
11.	University accounting curricula should be revised to enable students gain exposure to practical applications of IAS/IFRS and ISA.	NAA	Implemented
12.	Improve ICAN capacity to comply with the IFAC membership obligations (a) ICAN should update the Nigerian Code of Ethics in line with the IFAC Code. (b) ICAN should require firms to implement a quality control system in accordance with the IFAC International Standard on Quality Control. (c) ICAN should develop its own quality assurance system to ensure that auditors comply with applicable auditing and ethical standards and independence requirements.	ICAN	(a) Implemented (b) Implemented (c) Implemented
13.	Strengthen capacity of the regulatory bodies and review adequacy of statutory enforcement provisions. These bodies include Registrar of Companies at the Corporate Affairs Commission, Securities and Exchange Commission, Nigeria Stock Exchange, National Insurance Commission,	Regulatory bodies	Partially implemented

	Country Action Plan	Led by	Status as of February 2011
	and Non-Bank Financial Institutions Office in the Central Bank of Nigeria.		
14.	Strengthen ANAN capacity to comply with IFAC requirements for professional accountancy bodies.	ANAN	Partially implemented

[/a] Draft FRC Bill sits before the National Assembly awaiting passage into law.
[/b] Government in September 2010 adopted IFRS with effect from January 1, 2012, under a phased program.

III. INSTITUTIONAL FRAMEWORK

9. This section sets out emerging strengths and weaknesses in institutional framework that underpin accounting and auditing practices, with focus on developments since 2004.

A. Statutory Framework

10. **The statutory framework underpinning corporate accounting and auditing practices in Nigeria has not changed significantly since the 2004 ROSC A&A review.** Among major areas of change has been repeal of the Investments and Securities Act, 1999, replaced with the Investment and Securities Act, 2007. Section 63 of the Act provides for an auditor to issue a statement in the audit report with regard to the existence, adequacy, and effectiveness or otherwise of the internal control system of the public company. The Central Bank of Nigeria Act, 1991 was also repealed and replaced with the Central Bank of Nigeria Act 2007. Section 43 of the Act provides for establishment of a Financial Services Regulation Coordinating Committee to co-ordinate the supervision of financial institutions; the reduction of arbitrage opportunities, usually created by differing regulation; and the supervision standards among supervisory authorities, CBN and NDIC. Lastly, sections 52-55 of the Companies Income Tax Act (as amended in 2007) require every company operating in Nigeria, on a yearly basis whether or not it is liable to pay tax, to file returns of its income together with its audited accounts to the Federal Inland Revenue Service (FIRS). Furthermore, the FIRS Act 2007 requires the director or secretary of a company who files returns to attest that the returns contain a true and correct statement of the amount of its profit.

11. **The overarching Nigerian law for corporate accounting and auditing practices is the Companies and Allied Matters Act (CAMA) 1990.** Provisions of CAMA include requirements for auditing, accounting records, publication of financial statements, and annual returns. It specifies the form and content of financial statements. It also provides for the Registrar of Companies at the Corporate Affairs Commission to monitor compliance with these requirements and specifies penalties for companies and their officers in cases of noncompliance. The liability of auditors for negligence in the performance of his duties is also specified. The CAMA requires that financial statements comply with the Statement of Accounting Standards (SAS) issued from time to time, by the Nigerian Accounting Standards Board (NASB); and that audit be carried out in accordance with the generally accepted auditing standards. The CAMA requires an annual statutory audit of every company.

12. **The requirements of CAMA 1990 fall short of current international good practice.** The CAMA prescribes the format and content of company financial statements. This imposes limitations on corporate financial reporting. The Government of Nigeria in September 2010 approved conversion to IFRS, effective January 1, 2012, under a phased program. The CAMA

requirements are not in line with IFRS. The CAMA requires, for example, that the historical cost accounting rules be applied and financial statements comply, in form and content, with requirements of Schedule 2 of the Act; and with the accounting standards laid down in the NASB-issued SAS, provided that such accounting standards do not conflict with the provisions or Schedule 2 of CAMA. These CAMA requirements conflict with IFRS requirements.

13. **The laws regulating statutory audit are covered in CAMA 1990; Institute of Chartered Accountants of Nigeria (ICAN) Act, 1965; and Association of National Accountants of Nigeria (ANAN) Act, 1993.** The CAMA specifies the qualification, appointment, remuneration, termination, and powers of the auditor. The CAMA requires each company to establish an audit committee. The CAMA provides for attendance of the auditor at any general company meeting, receipt of notices and other communications relating to any general meeting, and opportunity to be heard at such meeting on any part of the meeting that concerns them as auditors. The CAMA 1990 (as amended) allows only ICAN members to be appointed as statutory auditors.

14. **The Central Bank of Nigeria Act and the Banks and Other Financial Institutions Act, 1991, designate the Central Bank of Nigeria as the main regulator of banks and non-banking financial institutions.** These Acts contain provisions on audit and financial reporting by banks and non-bank financial institutions. The Central Bank specifies the minimum information disclosure requirement applicable to banks financial statement. Banks submit data online through the electronic Financial Analysis and Surveillance System (e-FASS) to CBN and NDIC on a regular basis (daily, weekly, mid-month, monthly, quarterly, semi-annually, and annually). The Central Bank carries out both on-site and risk-based, off-site bank supervision; this responsibility is shared with the NDIC. The appointment of a bank statutory auditor is subject to the approval of the Central Bank. According to the current code of corporate governance issued by the Central Bank, a bank may appoint an auditor for a maximum period of 10 years. Collaboration between the Central Bank and statutory auditors includes statutory auditors sending domestic/management reports directly to the Central Bank; quarterly, structured meetings with statutory auditors; and attendance of statutory auditors at exit meetings to discuss CBN on-site examination findings.

15. **Under the Insurance Act of 2003, the National Insurance Commission (NAICOM) regulates financial reporting by the insurance companies.** The CAMA and the Insurance Act establish the financial reporting and auditing requirements of insurance companies. Insurance companies file quarterly returns 30 days after the end of the quarter and annual returns not later than June 30 of each year to the NAICOM. The process of appointing statutory auditors of insurance companies includes approval by the NAICOM. Statutory auditors are appointed for a maximum period of 5 years. Resignation or termination of a statutory auditor need not be reported to NAICOM. The NAICOM performs both off-site and on-site review of compliance with accounting and auditing requirements in the course of carrying out supervisory activities.

16. **The Securities and Exchange Commission (SEC) and the Nigeria Stock Exchange (NSE) regulate listed companies.** The financial reporting and disclosure requirements for listed companies are specified in the Investment and Securities Act, 2007. The Securities and Exchange Commission is the apex of regulatory bodies of the Nigeria capital market. Listed companies submit audited annual accounts and report half-yearly financial performance, interim/quarterly financial statements, quarterly earnings forecast, and half-yearly returns on unclaimed dividend warrants to the Securities and Exchange Commission. The quarterly financial statements, presented

in a prescribed format, do not need auditing. Statutory auditors of listed companies are registered with the Securities and Exchange Commission. The Nigeria Stock Exchange supervises the securities market operations. Required submissions to the Stock Exchange include annual reports due 90 days after fiscal year-end and quarterly report due 45 days after end of each quarter.

17. **As per CAMA requirements, the Registrar of Companies keeps records of returns submitted by public and private companies.** Companies' statutory financial statements are required to be filed annually with the Corporate Affairs Commission (CAC) within 42 days at conclusion of the annual general meeting. Documents to be filed vary for small and unlimited companies and big companies. In most cases, despite penalties for noncompliance, many companies do not comply with the deadlines. However, enforcement is weak. Of the 827,000 private limited companies and 42,500 public limited companies in the CAC books, a sizeable number are believed to be dormant. The Corporate Affairs Commission does not have the mandate to delist dormant companies. Manually prepared documents and not electronic copies are kept at the Corporate Affairs Commission. The unavailability of electronic documents hampers timely availability of statutory financial statements to external parties.

18. **The National Pension Commission (PENCOM) formulates and oversees pension policy in Nigeria as well as regulates and supervises the private pension industry.** The new organizational and regulatory approach adopted by the private pension industry in Nigeria — the primary service providers, Pension Fund Administrators, and Pension Fund Custodians; and their regulator, PENCOM — was established following major reforms initiated in 2004. Licensed operators submit daily reports, monthly reports, and annual accounts to PENCOM. Audited financial statements are subjected to review by PENCOM before publication. Pension Fund Administrators submit two sets of financial statements — one for the Pension Fund and other for the company.

19. An overview of the accounting, auditing, and publication requirements and standards of Nigeria statutory framework is summarized in Table 3.

Table 3: Overview of current accounting, auditing, and publication requirements for major entities in Nigeria

Type of entity	***Regulatory agency***	***Accounting standards***	***Audit requirements***	***Audit firm rotation***	***Publication***
Listed companies	SEC, NSE, CAC	SAS (IFRS with effect from 2012)	NSA issued by ICAN	None	Complete audited financial statements published on company website and National Newspaper.
Banks	CBN	CBN prudential guidelines and SAS (IFRS with effect from 2012)	NSA issued by ICAN; Appointment of auditor subject to CBN approval	New audit firm every 10 years	Annual F/S with notes published in 3 national newspaper; quarterly unaudited abridged financial statements without notes published in 3 national newspapers.
Pension Fund	PENCOM.	SAS (IFRS with effect from 2012)	NSA issued by ICAN	None	Completed audited financial statements published on company website.

Insurance companies	NAICOM	SAS (IFRS with effect from 2012)	NSA issued by ICAN experience	New audit firm every 5 years	Company publishes annual balance sheets and income statements for each regulated entity.
Non-banking financial institutions	CBN	SAS (IFRS with effect from 2012)	NSA issued by ICAN	None	Company publishes annual balance sheets and income statements for each regulated entity.
Credit societies/ cooperatives	None	SAS (IFRS with effect from 2012)	Yes	None	Company Publishes annual balance sheets and income statements.
State-owned public enterprises	None	SAS (IFRS with effect from 2013)	No	None	CGRP publishes complete financial statements with notes, but without auditor's report, on its website.
Non-listed companies	None	SAS (IFRS with effect from 2013)	Yes	None	Company publishes annual balance sheets and income statements.

B. The Profession

20. **There are two self-regulating, professional accountancy bodies in Nigeria: the Institute of Chartered Accountants of Nigeria (ICAN) and the Association of National Accountants of Nigeria (ANAN).** The ICAN Act, 1965, and ANAN Act, 1993, mandate that ICAN and ANAN, respectively, regulate the accounting profession in Nigeria. At present there is no separate independent statutory regulator of the audit profession. The FRC Bill under consideration by the National Assembly elaborates provision for establishment of the statutory regulator. The ICAN Act regulates the practice of auditing and accounting by ICAN members. The ICAN Act specifies the requirements for registration of accountants, which include completing a professional accountancy education program, passing the qualifying membership examination, and completing a 36-months internship with a firm of chartered accountants. The ANAN Act determines the standard of knowledge and skills required of persons seeking to become ANAN members. The ANAN Act includes requirement for qualifications for membership and issue of practicing certificates. Currently, ANAN admits graduates of accounting and other social science disciplines (especially business and economics) into its accountancy college for a 9-months program. After this program, students are expected to undergo a 24-month accountant-in-training assignment in any sector of the economy before enrolling as an ANAN member.

21. **The ICAN has full IFAC membership, and its members dominate accounting and auditing services in the Nigerian private sector.** The ICAN has 31,500 registered members, of which 6,000 are in public practice. There are 2,000 audit firms in Nigeria with 1,850 sole practitioners. Under the current system, ICAN registers only individuals as practicing auditors, and there is no arrangement in place for registering audit firms in the country. The ANAN members are mostly employed in the public sector. The ANAN membership stands at 15,720, with 500 in public practice. The ANAN is moving toward IFAC membership; however, further steps will be necessary to successfully obtain IFAC membership.

22. **A shortage of qualified accountants persists in the private sector.** There are about 827,000 private limited companies and about 42,500 public limited companies in Nigeria. With ICAN membership at 31,500, a significant gap exists between demand for and supply of qualified professional accountants in Nigeria.[6] In a bid to address the shortage, ICAN in 2005 changed its professional qualification program to allow the warehousing of credits for subjects passed rather than the previous wholesale pass of each stage of the professional examination.

23. **Since 2005, IFAC has conducted the self-assessment Member Body Compliance Program to monitor compliance with the requirements of the Statements of Membership Obligation (SMO) among its membership.** In addition, the Compliance Program encourages its members and associates to make further progress with respect to the SMOs that cover quality assurance; professional accountancy education; adoption and implementation of international accounting, auditing, and ethics standards; and investigation and discipline. Having completed the self-assessment part of the Compliance Program, ICAN developed a detailed action plan to describe its planned activities to address the SMO requirements; it is now implementing them. The ICAN needs to make continuous efforts to strengthen its current arrangement of quality review for ensuring compliance with International Standards on Quality Control (ISQC-I) for the practicing members (i.e., SMO 1, *Quality Assurance*) and also devise strategies to serve the public sector better, and thus contribute to ensuring compliance with the SMO 5, *International Public Sector Accounting Standards and Other IPSASB Guidance*. With regard to SMO 2, *International Education Standards for Professional Accountants and Other IAESB Guidance*, the ICAN professional curriculum does not adequately focus on the practical application of accounting and auditing standards. Thus, in reality, professional accountants are deprived of adequate skills and training. Although the ICAN largely complies with most other SMO requirements, further improvements in ICAN capacity would create a better compliance environment. At present, the ANAN has not put in place an institutional arrangement for meeting the specified IFAC obligations but needs to develop a clear plan that would demonstrate its commitment to adequately meet the IFAC requirements.

24. **The auditors of many small and medium-size enterprises (SMEs) are auditing the same financial statements that they have prepared.** Some small and medium-size enterprises do not have qualified accounting personnel. Unqualified and inexperienced accounting staff are unable to prepare financial statement in line with relevant accounting standards. The CAMA imposes audit requirement on all registered companies, including small and medium-size enterprises. In fulfillment of this obligation, the auditor is also preparer of the accounts. This practice violates the auditor's independence rule and the quality of audit. At present, the audit threshold is not in existence in Nigeria.

25. **The big-4 audit firms dominate the practice in Nigeria.** These international, networked firms perform the audit of most of the listed companies. Professionals working in small and medium-size practices encounter challenges in keeping abreast with developments in accounting and auditing. The small and medium-size practices are handicapped by lack of access to current literature on applicable accounting and auditing standards. This situation adversely affects the quality of audit in the country. In order to encourage establishment of viable audit firms with adequate human and financial resources and to improve competitiveness in the audit market, ICAN

[6] The IFAC has defined a professional accountant as a member of a member-body of IFAC.

encourages merger of sole practitioners. In this regard, ICAN has created a portal to assist firms willing to merge. In the recent past, three successful mergers have taken place. However, most small and medium-size audit practices still prefer to remain as sole practitioners.

26. **There is no statutory condition that requires practicing accountants to take professional liability insurance; in fact such insurance policies are not available in Nigeria.** Nigeria's relevant laws do not provide for significant penalties against negligent auditors. This tends to limit auditor's accountability and in many cases has created an environment of unconcern toward risks of malpractice suits by auditors. Nigeria has not yet experienced any litigation against auditors.

C. Professional Education and Training

27. **Professional accounting and auditing education in Nigeria needs to be further strengthened to ensure future practicing accountants acquire adequate professional capabilities and competency and are sufficiently qualified to undertake their activities.** The entry requirements to become an ICAN-licensed auditor generally comply with IFAC-issued International Education Standard (IES) 1, *Entry Requirements to a Program of Professional Accounting Education,* issued by IAESB of IFAC. However, the ROSC Team observed an uneven quality in university-conducted accounting education in Nigeria. The scope of the current ANAN certification program does not provide future auditors with sufficient knowledge to undertake an audit. The educational preparation of future accountants for professional certification requires further improvement in preparing ANAN for IFAC membership.

28. **The ICAN-required practical experience falls short of IES 5, *Practical Experience Requirements*.** Candidates are required to have a minimum of 36-months experience in their area of expertise in accordance with IES 5. However, there is no written guidance for employers, mentors, and trainees regarding the program of practical experience that clarifies their roles and responsibilities, nor a mechanism for approving employers as suitable for providing the appropriate experience for trainees. The ANAN practical experience requirement, which is currently 24-months long, would need to be further extended and strengthened.

29. **The ANAN-conducted professional accountancy examination falls short of the IES requirements on assessing professional capabilities and competence.** In order to meet the reliability and validity of IES 6, *Assessment of Professional Capabilities and Competence,* future accountants should be prepared with sufficient range of professional knowledge; professional skills; and professional values, ethics, and attitudes. The ANAN examination system does not seem to test underpinning theoretical knowledge and its practical application, including judgments by accountants in real-life circumstances as per IFAC requirements. The ROSC Team reviewed the ANAN curriculum and inferred that it primarily focuses on technicalities of accounting and auditing. The ANAN examination does not test knowledge with regard to professional skills, values, and ethics. Also, it does not focus on practical implementation issues of applicable standards.

30. **Accountancy education lacks adequate exposure of practical application of standards.** In discussions with the ROSC Team, many stakeholders expressed concern that new accountancy professionals lack exposure of the practical application of accounting standards, adequate level of

communication skills, and aptitude in forming judgment in applying accounting policies for measurement and disclosure of financial information. The stakeholders believe that university graduates do not have adequate levels of practical knowledge and are not prepared to deal with the challenges of discharging their professional responsibilities. In most cases, the employers have to spend substantial time and resources to train newly hired accountants to begin their assigned jobs.

31. **The accounting and auditing curricula in Nigeria are not harmonized among universities and are generally not current with International Education Standards.** Nigerian universities and polytechnics have not made effort to establish common, minimum requirements for courses on accounting and auditing. The accounting curricula are mostly restricted to accounting technicalities and basic procedural aspects of auditing. Moreover, most accounting textbooks lack adequate focus on current international accounting and auditing standards and practice, in particular the practical application of accounting and auditing standards. The various universities visited by the ROSC Team have little involvement with the international professional accounting organizations; for example, none of them subscribe to the updated IASB publications, and none have made attempts to implement IES recommendations regarding accounting and auditing education.

32. **Within the structure of professional examination in Nigeria, there is no distinction between the accounting qualification and auditing qualification.** The professional examination is not designed to adequately achieve IES 8, *Competence Requirements for Audit Professionals*. The IES 8 treats the auditor qualification as a follow-up to the qualification of a professional accountant and specifically states that audit professionals need an “advanced level” of knowledge in auditing financial statements. Its additional requirements on education and experience are not yet covered in Nigeria. The ICAN and ANAN therefore need to look at required upgrading to advance the curricula and examination process. Auditors should be required to pass an additional examination for obtaining the practice license.

33. **Continuing professional development (CPD) for practicing accountants is mandatory, but there is no uniform guidance in organization and delivery.** Professional accountants are required to participate in a CPD program for a total of 90 hours within 3 years, but current CPD arrangements appear to be inadequate to develop or maintain sufficient knowledge and professional skills with regard to modern accounting and auditing practices. Moreover, many CPD seminars lack clear focus on practical implementation aspects of applicable accounting and auditing standards and would need to be updated in an ongoing manner if they are to ensure taking into account new and revised standards.

D. Setting Accounting and Auditing Standards

34. **Under the Nigerian Accounting Standards Board Act of 2003, the NASB sets local accounting standards.** Compliance with NASB-issued Statement of Accounting Standards is mandatory under CAMA. The Government of Nigeria in September 2010 approved conversion to IFRS as the basis for the preparation of statutory financial statements in Nigeria, to be effective January 1, 2012. To guide the adoption of IFRS, a road map has been prepared (see Figure 1). The IFRS adoption is planned to be a phased transition over 3 years commencing with public listed entities and significant public interest entities in Nigeria by 2012, followed by other public interest entities in 2013 and small and medium-size entities in 2014. To ensure effective adoption of IFRS,

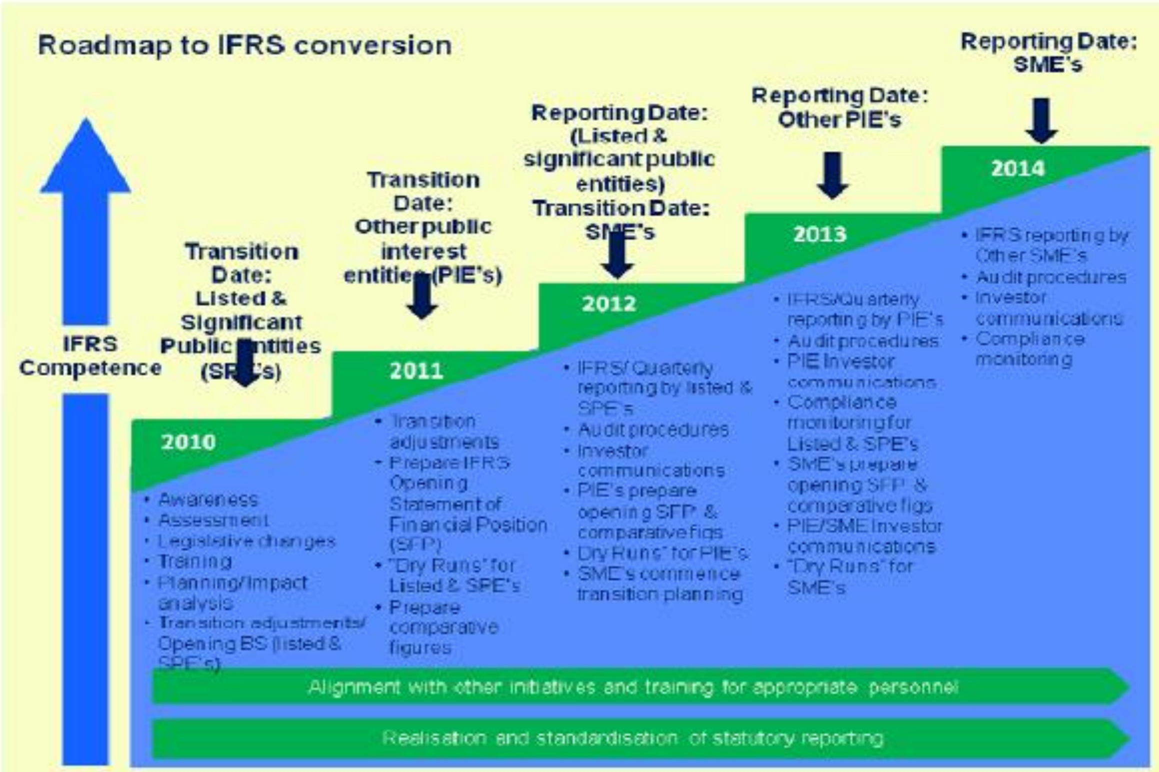
the Committee on Road Map in their report recommended the following:

- Amendment of laws and regulations — CAMA 1990; Banks and Other Financial Institutions Act, 1991; and Investment and Securities Act, 2007 — that have one provision or other impacting on financial reporting in order to ensure uniformity and remove conflicts and ambiguity;
- Passage and signing the enactment of the FRC Bill;
- Enforcement of IFRS vested in one body; and
- Creation of IFRS Center of Excellence.

The road map indicates milestones and timelines to be followed over the 3-year period. However, some of the milestones for 2010 have already been missed. The various regulators are providing guidance on how companies under their watch should comply. A properly coordinated effort will be more appropriate. The NASB, which should provide the required coordination/leadership, is constrained by its resource limitations. The CBN has commenced implementing a plan to support IFRS conversion in the banking sector which other regulators could follow under the regulators forum.

35. **The ICAN and ANAN are standard-setters for auditing practice in Nigeria by virtue of their respective acts, and both have been issuing standards accordingly.** Two sets of auditing standards exist in Nigeria. The ICAN mandates compliance with Nigeria Standards on Auditing, which it issues. However, the local members of international accounting firm networks issue their audit opinion in line with ISA. The ICAN lacks the mechanism to enforce compliance with its standards. The ICAN-issued standards incorporate local specificities, complying only to some extent with ISA. The last standards issued by ICAN were in 2009; what exist at present are exposure drafts. With the clarified ISA there are differences between the Nigeria Standards on Auditing and ISA. The ANAN members in public practice apply the ANAN-issued auditing standards. A legal body responsible for mandating auditing standards in Nigeria is necessary to address the issue of multiple standards and monitoring and enforcement of compliance with auditing standards.

Figure 1: IFRS Conversion Road Map Diagram



Source: *Report of the Committee on Road Map to the Adoption of International Financial Report in Nigeria, 2010.*

E. Ensuring Compliance with Accounting and Auditing Standards

36. **The mechanism for monitoring and enforcing requirements on accounting and financial reporting is provided for in the CAMA 1990, and other acts related to the powers and responsibilities of regulators**. The CAMA empowers the Registrar of Companies at the Corporate Affairs Commission to monitor compliance with its financial reporting requirements. The Corporate Affairs Commission does not effectively fulfill this function. Generally, returns are not filed within the stipulated deadline while returns for some companies, especially private and non-listed public companies, are not readily available. The CAMA requires the audit committee to review audited financial statements and report to the shareholders. However, audit committees' capacity to monitor remains largely unknown. The CAMA is outmoded regarding penalties for noncompliance. This has resulted in weaker monitoring and enforcement activities with regard to application of the accounting and financial reporting requirements.

37. **The Nigeria Stock Exchange does not have any monitoring and enforcing mechanism with respect to accounting and disclosure requirements.** At present, NSE monitoring efforts are primarily focused on tracking timely issuance and filing of the financial statements. Even with these efforts there are companies with overdue filing of financial statements. At the Stock Exchange, the available financial statements are not reviewed for ensuring compliance with accounting standards and disclosure requirements. The NSE monitoring and enforcement mechanism is very weak. The Nigeria Stock Exchange is undergoing a transformation process, which is expected to enhance its institutional capacity.

38. **The Securities and Exchange Commission in 2007 established the Financial Standards and Corporate Governance Department to review financial statements of all the publicly traded companies for ensuring compliance with the accounting standards and disclosure requirements.** However, this initiative remains at the nascent stage. The officials responsible for monitoring and related activities lack the adequate knowledge on practical aspects of applying IFRS. The capacity of the Financial Standards and Corporate Governance Department is weak. Some enforcement actions taken by the Security and Exchange Commission include sanctioning one publicly traded company and its auditor for resorting to "creative" accounting, and penalizing a number of companies for delay in filing of financial statements.

39. **The ICAN has commenced conducting a quality assurance review of professional practice of audit firms and individual auditors; however, the quality control process is at an early stage and falls short of international good practice.** Reviewers for the exercise are ICAN members selected on a competitive basis. The Director for Practice Monitoring coordinates the exercise. A pilot review involving 29 small and medium-size audit firms was conducted in 2010. Experience shows that most of the audit firms are unwilling to submit to the review. The review outcome does not include sanctions, and recommendations are largely persuasive. The ICAN should make efforts to ensure this initiative is in compliance with SMO 1, *Quality Assurance*. Due to the absence of independent audit oversight, Nigeria does not yet have an effective audit regulatory framework. There is a need to put in place an effective mechanism for enforcement of rules and regulations for strong monitoring, control, and surveillance, as well as a quality control system.

40. **For the banking sector, the Central Bank of Nigeria has strengthened its enforcement of financial reporting requirements.** The Central Bank regulates accounting requirements for prudential regulatory reporting of banks as well as non-banking financial institutions. In this context, the Central Bank monitors adherence to financial reporting requirements mainly with regard to loan loss provisioning and other issues that affect capital adequacy of the regulated entities. The Central Bank does both off-site and on-site examinations and gives priority to checking compliance with prudential requirements. The Central Bank reviews and approves the audited financial statement before they are published. Banks now submit their returns through the electronic Financial Analysis and Surveillance System (e-FASS), and plans are underway for risk-based banking supervision. According to the CBN half-year economic report as of end June 2010 and released the first week of March 2011, an assessment of the banking sector, based on *capital adequacy, asset quality, management, earnings, and liquidity* (CAMEL) during the review period, showed that none of the 24 banks was rated in the top grades. Half of the banks were rated "average" while the remaining ones had poor ratings. Also, the average Capital Adequacy Ratio of the banks was below the stipulated minimum of 10.0 percent.

41. **Compliance with financial reporting requirements of insurance companies is the responsibility of the Supervision and Inspectorate Division of the National Insurance Commission.** There is a whole range of sanctions that can be applied for noncompliance with accounting and auditing requirements. However, these sanctions do not appear to be effective. Also, the capacity of NAICOM to monitor compliance is inadequate.

42. **The Nigerian Accounting Standards Board is mandated to monitor and enforce**

compliance with accounting standards. The NASB writes to companies requesting their financial statements for review. The review is conducted using checklists developed for each SAS. Issues of noncompliance are conveyed to the company with a request that the auditor accompanies the company to the inspection meeting. The NASB has improved upon its monitoring and enforcement function thus becoming prominent in the discharge of this responsibility. Arising from its monitoring, some companies and their auditors have been sanctioned for manipulating accounting principles. The NASB still lacks adequate financial and human resources to ensure compliance by the many companies in Nigeria in general and public interest entities in particular.

43. **For non-listed entities, in both financial and non-financial sectors, there is no system to effectively ensure that they adhere to applicable standards in their financial statements.** The absence of monitoring and enforcement of financial reporting requirements for the non-listed entities and especially those in unregulated sectors poses a significant threat in ensuring good governance and developing a sound financial architecture in Nigeria. Many of the non-listed entities, including state-owned enterprises, represent significant public interest.

IV. ACCOUNTING STANDARDS AS DESIGNED AND PRACTICED

44. **The Nigerian Statement of Accounting Standards were developed by the NASB on the basis of IAS/IFRS**. The NASB has not issued any instructions on what to do when there are no SAS counterparts of IAS/IFRS. Companies are encouraged to apply international good practice (e.g., IAS/IFRS) where SAS do not exist. It is worth noting that there are 38 applicable IAS/IFRS; however, the existing 30 SAS cover only about 50 percent of the IAS/IFRS areas. The major companies, including banks and insurance companies, generally claim that they have used the requirements of IAS/IFRS in areas not covered by SAS.

45. **Since the decision to adopt IFRS in Nigeria was taken at the highest level of Government, this development was expected to facilitate smooth implementation**. However, most of the preparatory arrangements outlined in the road map have yet to be achieved. For instance, the road map prescribed that adequate public sensitization be carried out beginning from 2010 to enable the preparers and users of financial statements, regulators, auditors, investors, and other relevant stakeholders to be properly educated. The ROSC Team in discussions with relevant stakeholders learned this has not been done.

46. **Evidence suggests a lack of adequate capacities to prepare IFRS-based financial statements**. A knowledge gap on IFRS-based financial reporting appears to be a significant challenge faced by the accountancy profession in Nigeria. During the due diligence mission in discussions with company management, accountants, and auditors, the ROSC Team found that some companies might not have adequate resources or ability to prepare IFRS-based financial statements. It is possible therefore that in these cases the auditors might either prepare or provide substantial assistance with the preparation of such financial statements. This however raises a significant independence issue.

47. **Financial statements often include standardized wording, which may not relate to the specific events and circumstances of the concerned corporate entity.** The standardized wording is usually drawn from model financial statements provided by the audit firms. In most cases, the

standardized wording is used for describing accounting policies for events and transactions that are not relevant to the financial reporting of the concerned entity. The users of financial statements generally are of the view that using standardized wording reflects a lack of knowledge and understanding of complex accounting requirements, including IFRS, by the preparers of financial statements and generally reduces the relevance of those financial statements.

48. **Information on "compliance gaps" demonstrates weaknesses of corporate financial reporting.** The review of published financial statements, conducted by the ROSC Team, has revealed compliance gaps, the so-called difference between applicable accounting standards and actual practice. The review mainly involved an examination of 40 sets of financial statements of major listed companies against a checklist of selected disclosure requirements under the NASB-issued Statement of Accounting Standards. In areas where SAS do not exist, the relevant IAS/IFRS disclosure requirements have been included in the checklist. The review also involved interviews with experienced corporate accountants, practicing auditors, academics, members of professional bodies, and regulators. The exercise has shown noncompliance with important disclosure requirements. It is worth noting that the review mainly focused on the disclosure requirements; no attempt was made to examine the books of account of the companies and/or audit working papers in order to dig deep into the recognition and measurement issues. Although a range of noncompliance was detected, a few examples are presented below:

- **Disclosures.** Many companies avoided full disclosure of information in published financial statements as per requirements of the applicable Statement of Accounting Standard. More importantly, the observed accounting policies in line with the SAS requirements, are hardly presented in a proper manner.

- **Related party transactions.** Detailed disclosures in line with the requirements of the relevant accounting standard were generally absent in the reviewed financial statements. For instance, the ownership structure of many companies suggested that related parties and related party transactions existed, but the notes to the financial statements of these companies showed either very limited or no disclosures with regard to related parties and related party transactions.

- **Revenue recognition.** Many companies did not properly disclose the accounting policy on revenue recognition. In this context, some analysts and other users of financial statements in the country have opined that many companies resort to overstatement or understatement of revenues in order to show the accounting profit at a desired level.

- **Employee benefits.** Although many companies have employee pension plans, almost all of them failed to disclose information required by the relevant accounting standard. No disclosure was made as to whether actuarial or any other forms of valuations had been made to quantify outstanding liabilities for employees' post-employment benefits. According to the knowledgeable accountants and auditors in the country, in many companies the full liability for employee benefit expenses is not recognized on an accrual basis.

- **Segment reporting.** Most companies that apparently had business segments and geographical segments did not comply fully with the segment reporting requirements.

Details were not provided for revenue, operating profit, total assets, and total liabilities of different segments.

- **Leases**. Misclassification of leases is a common practice. The leases, which are essentially finance leases, are treated as operating leases. This misclassification improves the liability side of the balance sheet and creates more favorable borrowing capacity of the company.

- **Impairment of assets.** It is a common practice not to disclose whether impairment tests have been performed as per requirements of the applicable accounting standard. Although some reviewed financial statements made reference to an impairment review, all the required disclosures on impairment adjustments and related matters were not found in most of the financial statements.

- **Financial instruments**. Except in the case of a few banks, appropriate accounting and disclosures for financial instruments are rarely found in the financial statements of the corporate entities.

- **Provisions, contingent liabilities, and contingent assets**. In most of the financial statements, the explanatory notes were not in compliance with the requirements of the applicable accounting standard. With inadequate information, this could prevent the user of the financial statements from properly assessing the consequences of a contingency.

- **Consolidated financial statements**. It is a common practice not to present information on the basis of consolidation of subsidiaries, and nature of relationship between parent and subsidiary. Many companies often fail to consolidate all the subsidiaries without providing valid reasons for this.

V. AUDITING STANDARDS AS DESIGNED AND PRACTICED

49. **The ICAN-mandated auditing standards fall short of the requirements of clarified ISA**. The ICAN has issued 30 Nigerian Standards on Auditing through adaptation of ISA to suit local circumstances. As a result, the Nigerian Standards on Auditing are not fully comparable with the requirements of the original ISAs. The IAASB (IFAC) revised the original ISAs, which were reference points of Nigerian Standards of Auditing, at the conclusion of the "clarity project" in December 2009. At present, there are 36 clarified ISAs that need to be adopted and implemented in Nigeria. However, the Nigerian Standards on Auditing have not yet been updated to reflect the requirements of the clarified ISA. The differences between Nigerian Standards on Auditing and clarified ISA are such that an audit performed in accordance with Nigerian Standards on Auditing is likely to provide much less assurance than an audit performed in accordance with current ISAs. The current practice of adapting ISA for Nigerian Standards on Auditing does not appear to be efficient way of setting national standards and is not helpful for developing a strong auditing profession and financial information process. All requirements of currently applicable ISA need to be mandated through full ISA adoption.

50. **The quality of statutory audits is uneven**. From the review of audited financial statements and discussions conducted by the ROSC Team with sole practitioners, medium- and large-size audit

firms, NASB, and other relevant regulatory bodies, specific issues surfaced that affect the average quality of auditing practices in Nigeria. It was found that the degree of compliance with the applicable auditing standards differs among audit firms of different sizes. The audit firms that belong to the international networks generally follow ISA requirements. However, due to differences of opinion over the spirit of certain auditing standards, actual application in local environments tends to differ in different firms. Moreover, intense work pressures force many large audit firms to comply with audit standards more in form than in substance. Some audit quality issues recognized in firms of all sizes include the following:

- Regarding implementation of the standard on ***going concern***, it seems that the shortcomings in effective compliance with this standard sometimes significantly affect the quality of financial statements of some public interest entities.
- Regarding ***risk assessment and internal control***, in many cases proper steps are not taken for checking whether the controls were functioning throughout the whole accounting period.
- It is widely believed by the key stakeholders that the auditing standard regarding ***related parties*** does not receive the attention it deserves, taking into account that many of the public interest entities in the country have related party relationships and related party transactions.
- Local circumstances constrain the use of ***external confirmation procedures*** as an effective tool in obtaining relevant and reliable audit evidence.
- A common practice in audit practice in Nigeria is low-balling ***fees***, or quoting an artificially low fee in order to win an audit contract. This is done by the bidding firm on the assumption that their future fee for expected non-audit work from the same client would compensate for the “low” quoted fee for the current audit.
- The lack of effective ***communication*** between incoming and outgoing auditors of an entity affects the quality of audit.
- In many cases, inadequately supervised trainee accountants, having very limited exposure to the ***theory and practice*** of auditing and without sufficient knowledge of client’s business, carry out important audit activities. This has serious impact on the quality of audit.

51. **The small and medium-size practices often find it difficult to bear the cost of implementing proper arrangements for audit quality control**. Generally, weak capacity adversely affects the quality of audit services provided by the small and medium-size practices in Nigeria. Some typical examples of noncompliance with audit standards by small and medium-size practices follow, prepared on the basis of information provided by the audit practitioners and the relevant regulators in Nigeria:

- Terms of audit engagement not agreed upon in writing;
- Inability to demonstrate knowledge of clients business;
- Absence of records of audit planning;
- Audit work carried out is not adequately recorded;
- Serious and consistent deficiencies in the extent and quality of audit evidence;
- No records of application of analytical procedures at both planning and overall review stage;

- No record of review of post balance sheet events;
- Written confirmation not obtained from management of the various matters;
- No record on how the firms ensured financial statements complied with the requirements of CAMA and SAS.

VI. PERCEPTIONS ON THE QUALITY OF FINANCIAL REPORTING

52. **As was the case in 2004, perceptions of the quality of financial reporting in Nigeria remain mixed at best, and most users consider that more efforts are needed to improve the quality of audited financial statements.** The ROSC Team interviewed a cross section of the users of financial statements, including the regulators and participants in the financial market. The users perceive the quality of financial statements having improved somewhat but still relatively weak overall. And there is a need to take some major steps for improving audit quality. Financial reporting by banks is perceived to have improved, in large part due to the fact that the banking supervisor has stepped up monitoring and enforcement activities. However, greater reliability of audit reports is still needed, and accountability of external auditors is viewed as inadequate.

53. **The adoption of IFRS to be effective January 1, 2012, is perceived to be a positive step that will facilitate investment and lending activities.** However, the market perceives there is a paucity of skills in using IFRS within the system since greatest numbers of accountants in Nigeria were trained on the basis of the Nigeria Statement of Accounting Standards.

VII. POLICY RECOMMENDATIONS

54. The policy recommendations outlined in this section emerge from the review of accounting and auditing practices in Nigeria, as well as valuable inputs received from the various key stakeholders, including leaders of the accountancy profession, experienced practitioners, regulators, academics, investment analysts, top management personnel of major corporations and financial institutions, and local and foreign investors. A holistic approach is adopted to design the principles-based policy recommendations in order to further strengthen the corporate financial reporting and auditing practices in Nigeria. The significance of these recommendations is building on existing systems — implementation of the recommendations should not jeopardize achievements of the framework and systems in place. The major focus of the policy recommendations centers around the following:

- Updating the *statutory framework* of accounting, auditing, and corporate financial reporting;
- Strengthening the capacity of *accounting and auditing regulatory body* for issuing, monitoring, and enforcing accounting and auditing standards;
- Building capacity of the *professional accountancy bodies* to function as modern professional organizations, and comply fully with the IFAC Statements of Membership Obligations;

- Enhancing capacity of the main *financial sector regulators* — banking regulator, securities regulator, and insurance regulator — to deal more effectively with matters relating to IFRS application by the regulated entities; and
- Improving *accountancy education and training*.

A. Statutory Framework

55. **Amend the Companies and Allied Matters Act, 1990.** The CAMA needs to be amended taking into account the important reforms that the Nigerian Government has introduced with regard to enhancing the quality of corporate financial reporting. The CAMA at present is based on the premise that the accounting and auditing practices in Nigeria should be based on nationally developed standards. The Government of Nigeria has already taken steps for building national financial architecture in line with internationally accepted standards and codes. Under such circumstances, there is an urgent need for including enabling provisions in the CAMA in order to facilitate implementation of IFRS and ISA. The regulations/guidelines for implementing the amended CAMA should also ensure that penalties for failure to comply with the applicable accounting standards and for failure to file financial statements with appropriate authorities are set at levels that can act as effective deterrents.

56. **Prescribe by accounting standards and not law the form and content of financial statements**. The forms and contents of financial statements should follow the requirements set by accounting standards and not by the law. Legislated accounting policies and disclosure requirements cannot keep pace with changes in standards, disclosures, and relevant international practices considering how amendments to the law are cumbersome and difficult to implement on a timely basis. In order to satisfy a regulatory body's specialized information needs, regulatory information should continue to be submitted under the requirements set by the concerned regulator (e.g., CBN, SEC, NAICOM), and the general purpose financial statement should follow IFRS or the national equivalent of IFRS — an international good practice. The Second Schedule of the CAMA that prescribes accounting policies with regard to issues that are covered by accounting standards should be discontinued in favor of the accounting standards issued by a legally established body responsible for setting accounting standards (as done currently by NASB).[7]

57. **Provide eligibility requirements for appointment of statutory auditor.** Since CAMA is the principal act governing affairs of a company, it should provide unambiguous direction on who can be appointed as a statutory auditor. The CAMA should also provide in a schedule the detailed requirements that must be met by an individual or firm to be recognized as a qualified auditor. The schedule should require that in order to be recognized as a qualified auditor an individual or a firm must obtain a "practicing certificate" from a professional accountancy organization established by law in Nigeria. The schedule may also require that the same professional accountancy organization should put in place arrangements for complying with the IES requirements on professional education, and training and should be set in line with high-quality governance principles. In addition, the professional accountancy organization should also have developed CPD requirements in accordance with the IES, be involved in the adoption of quality control standards for audit firms,

[7] The provisions of CAMA that require observance of "historical cost accounting principles" are not consistent with the IFRS requirements on fair value accounting. It is therefore necessary to exclude the accounting principles-related issues from CAMA and leave it to the legally established accounting standard setter.

contribute to the auditing standard-setting process, and have established effective mechanisms for investigating and disciplining their members for misconduct and breach of the rules. This is in line with international good practice.[8]

58. **Exempt small private companies from statutory audit requirement**. The CAMA should exempt the small private companies from statutory audit requirements. If the small companies are not required to present audited financial statements, they will be able to focus more on business expansion rather than spending time and resources for audit compliance purposes. The law should provide for establishment of statutory audit threshold. The threshold of audit exemption should be revised from time to time depending on changing circumstances. The Federal Inland Revenue Service should consider acceptance of the Accountants Report prepared by a professionally qualified accountant — not necessarily an auditor — for small private companies. The lower cost of preparing an Accountants Report, which certifies that financial statements are in agreement with the underlying records, would provide more reliable information for tax assessment.

59. **Take steps for enactment of the Financial Reporting Council (FRC) Bill**. The Government should take immediate steps for ensuring that the FRC Bill, which is under consideration of the National Assembly of the Federal Republic of Nigeria, is passed into law. This law will lead to the establishment of a comprehensive regulatory framework of corporate financial reporting in Nigeria. The Financial Reporting Council will be responsible for issuing, monitoring, and enforcing accounting and auditing standards. Additional focus of the Financial Reporting Council will be on corporate governance, actuarial standards, and valuation standards. In addition to enactment of the FRC Bill, there is a need to ensure uniformity and remove conflicts in financial reporting-related provisions of other laws, including the Nigerian Stock Exchange Act, 1961; Companies and Allied Matters Act, 1990; Nigeria Deposit Insurance Corporation Act, 2006; Banks and Other Financial Institutions Act, 1991; Investments and Securities Act, 2007; National Insurance Commission Act, 1997; Insurance Act, 2003; Companies Income Tax Act, 2004 (as amended); Petroleum Profit Tax Act, 2004; Pension Reform Act, 2004; and Federal Inland Revenue Service (Establishment) Act, 2007.

B. Accounting and Auditing Regulatory Body

60. **Make necessary arrangements for establishing and operationalizing the Financial Reporting Council immediately after enactment of the FRC Bill**. The NASB, which is the current regulator of accounting, should take preparatory steps for establishment and efficient functioning of the Financial Reporting Council as soon as the enabling bill is passed into law. The steps for developing FRC institutional capacity include the following:

(a) ***Developing a 5-year strategic plan for Financial Reporting Council to enhance its capacity in oversight and regulation.*** The NASB lacks adequate capacity to act with the authority expected of an effective regulator of accounting and auditing, or to act in an advisory capacity with its key stakeholders, including government and other financial sector regulators. Steps need to be taken, with the assistance of technical advisors having practical experience in a similar regulatory body in an industrialized country, to produce

[8] For example, see Schedules 10 & 11 of the UK Companies Act 2006.

a 5-year strategy that will show a strong technical authority and the transformative strengthening in the foreseeable future of the Financial Reporting Council.

(b) ***Arranging for high-quality review of financial statements of the public interest entities, which would entail:***

(i) Developing detailed workflows to be adopted by the Financial Reporting Council for carrying out activities in connection with the monitoring and enforcement of IFRS, with particular focus on the quality of financial reporting of corporate entities in general and public interest entities in particular, including:

- Development of a review program of annual financial statements based on risk assessment;
- When and how to conduct investigations concerning infractions in the financial statements that come to its attention, whether in the course of regular reviews or through complaints;
- Ensuring findings of the financial statements review are brought to the attention of other relevant financial sector regulatory authorities so that they can decide whether disciplinary or other sanctions should be applied;
- Guidance to the preparers of financial statements on steps to foster the consistent application of financial reporting requirements and to improve the compliance of corporate financial statements with reporting requirements;

(ii) Preparing detailed "how to" work manual(s) for conducting financial statement reviews.

(iii) Organizing hands-on training for FRC specialists on conducting financial statement review.

(c) ***Putting in place arrangements for high-quality practice review of the practicing auditors.***

61. **Address all key drivers that affect audit quality, including leadership, audit methodologies, competencies and skills, quality control, and external review, in the capacity-building activities to launch a strong Financial Reporting Council.** The objective of audit practice review is to ensure that the auditors comply with applicable quality control standards, auditing standards, and codes in order to provide reasonable assurance that the information presented in the audited financial statements is reliable. In order to meet this objective, the preparatory activities for building a strong Financial Reporting Council should include providing on-the-job training to relevant FRC staff and guiding local audit firms in the development of a quality control system for their auditing services by developing trainings on quality control and provision of implementation guidance and tools. These activities should also include delivering workshops and imparting hands-on training to local audit firms on improving quality of audit. Specific capacity-building activities include:

(a) ***Develop detailed workflows*** to be adopted by the Financial Reporting Council for carrying out activities in connection with the monitoring and enforcement of ISA and

ISQC, with particular focus on enhancing the audit quality of the corporate entities in general and public interest entities in particular;

(b) ***Develop methodologies*** for carrying out monitoring and enforcement activities with regard to auditing standards and codes of professional ethics, including samples of checklists, and penalty guidelines;

(c) ***Prepare detailed how-to work manuals*** for conducting audit quality reviews;

(d) ***Organize hands-on training*** for the FRC specialists on conducting audit quality reviews, specifically providing the FRC specialists with the technical and practical knowledge and experience (including on-the-job training) to evaluate efficiently the audit firms' quality assurance systems;

(e) ***Develop and disseminate guidelines*** for local audit firms on implementing in-house quality assurance systems (including those for smaller firms).

(f) ***Deliver quality assurance workshops*** to assist local audit firms in implementing their in-house quality assurance systems.

62. **The Financial Reporting Council should develop a collaborative arrangement with each of the key financial sector regulators — CBN, NDIC, SEC, and NAICOM.** The financial sector regulators rely on audited financial information in meeting their regulatory objectives; such information is, in many cases, used as the basis for determining regulatory capital. In order to be confident that the supervisory efforts and policy proposals based on audited financial information are appropriate, these regulators need to have confidence in the information provided in audited financial statements. This calls for a formal arrangement of collaboration between the accounting and auditing regulator (FRC) and the financial sector regulators. The arrangement, through memorandum of agreement or other instrument, should enable operational-level collaboration, including participation of individual financial regulator's inspector/supervisor in a FRC team, for conducting financial statement review of the respective regulated entities. This will enhance the quality of financial statement review of banks and other financial sector entities. Moreover, exchange of confidential information and the mechanism of effective enforcement of financial reporting requirements should be included in the collaboration arrangement.

63. **Take practical steps for implementation of the road map to IFRS conversion**. A Committee operating under the NASB prepared the road map in January 2010. It was adopted at the highest level of Nigerian Government in November 2010. Because of the delayed start, it was not possible to achieve the milestones for 2010. Moreover, the road map does not provide clear direction about the ways and means of achieving the milestones. In this context, institutional arrangements need to be put in place for enhancing technical capabilities of the preparers, auditors, and regulators with regard to the practical aspects of IFRS implementation. These efforts should address various issues concerning the challenges of proper compliance with the applicable IFRS requirements. These issues include:

(a) Arrangements for ensuring local availability of all IFRS exposure drafts and final versions. Teachers, students, trainee accountants, professional accountants, and all other interested parties should have easy access to IFRS and related IASB pronouncements, and be trained on new and revised IFRS on an ongoing basis, as needed, to assist them in understanding the standards and properly implementing them in the course of their activities.

(b) Ensure institutional arrangements/frameworks and due processes are adequate, flexible, and credible for robust review, development, and public scrutiny of international standards.

(c) Clarify the role of the NASB (FRC in future) in the new environment of international standard-setting and full observance in Nigeria by defining in particular the scope of its role, especially in relation to reviewing new and amended IFRS; providing comments on IASB-issued exposure drafts; and issuing interpretations, guidance, and the basis of conclusions.

(d) Ensure that the NASB/FRC is adequately resourced.

(e) Ensure that accounting standard-setting in Nigeria is aligned fully with IASB work plans and that IASB activities are monitored and tentative IASB decisions examined so that the applicable Nigeria accounting standards are issued at the same time as IASB-issued standards.

(f) Establish the basis on which accounting standards from other jurisdictions may be applied by preparers, where there may be no IFRS for particular types of transactions.

(g) Recognize that the IFRS are principles based and will require preparers to apply judgments when using the standards. The NASB/FRC should clarify the degree to which guidelines may be issued in Nigeria and the criteria on which these may be developed and issued.

(h) There should be awareness programs anchored by the Small and Medium Enterprise Development Agency of Nigeria (SMEDAN) and the professional accountancy bodies to sensitize the small and medium-size enterprises on the application of IFRS for SMEs.

64. **Make arrangements for mandating the application of current ISA and ISQC**. After establishment of the Financial Reporting Council, arrangements should be put in place for issuance of all the current ISA and ISQC, as mandatory auditing and quality control requirements in Nigeria. The Financial Reporting Council should establish mechanisms to review and adopt new and revised versions of ISAs and ISQC 1 in an ongoing manner. When IAASB updates existing standards and issues new standards, these should be immediately disseminated as local requirements. In order to facilitate this process, the Financial Reporting Council should issue locally the IAASB-developed exposure drafts and encourage the local audit practitioners to analyze the exposure draft and provide comments for transmittal to the IAASB. This process will enable Nigerian audit practitioners to gain advance exposure to an international standard while it is in the making. Until the establishment of Financial Reporting Council, the professional accountancy organizations, ICAN and ANAN, should require their members to comply with the current versions of ISA and ISQC 1.

C. Professional Accountancy Body

65. **Develop the accountancy profession to serve both private and public sectors of the economy**. There is broad consensus among key international stakeholders that a professional accountancy body’s members should have technical capabilities to provide professional services in both private and public sectors of the economy. From this perspective, both professional accountancy organizations, ICAN and ANAN, should create and maintain the technical and research capacity to meet the needs of both sectors. This would include, for example, developing

and maintaining expertise in both IFRS and International Public Sector Accounting Standards, as well as in auditing, ethics, and education standards as applied to both sectors. Increased focus by both the professional bodies on serving private and public sectors of the economy will greatly contribute to a sustainable and internationally respected accountancy profession, which is a critical feature of any well-functioning economy.

66. **Strengthen institutional capacity of ICAN with the help of a twinning partner to enhance the degree of compliance with IFAC Statements of Membership Obligations.** The rapidly changing environment and especially the latest global financial crisis, revealed new areas of need and highlighted the importance of strong audit profession, which is monitored and constantly upgraded. Particularly when rules of the game often change, a regular retooling and upgrading of the professional accountancy organization and knowledge of its professional members is crucial. For these reasons, ICAN needs to further strengthen its institutional capacity with the assistance of a twinning partner (a strong IFAC-member body) and make progress to further meet the SMO requirements. This phase of capacity building should be based on experience in Nigeria and elsewhere, and in particular focused on the following: (a) Completing the improvement of the accountancy education system in accordance with the International Education Standards issued in August 2009 as well as subsequent versions; (b) Adopting ISQC 1, which became effective mid-December 2009, and establishing ongoing mechanisms for adopting new and revised versions of ISQC; and (c) Observing results of the self-assessment by ICAN under the IFAC compliance program and its action plan, which was approved in May 2009.

67. **Build institutional capacity of ANAN, with the help of a twinning partner, to meet the requirements of obtaining IFAC membership**. In this regard, ANAN would need to put in place institutional arrangements for fulfilling IFAC membership requirements, focusing on various areas including strengthening accountancy education requirements, establishing mechanisms for adopting the requirements of the IESBA Code of Ethics on an ongoing manner, assisting with the implementation of accounting and ethics standards, and strengthening the investigation and disciplinary mechanisms. A twinning arrangement needs to be developed with a strong IFAC-member body with a mission and vision similar to that of ANAN. At the beginning of implementing the twinning program, the ANAN Council should work with the twinning partner to develop a strategic plan, within the framework of its enabling act. The strategic plan will guide and drive ANAN activities and priorities for a specified period. The strategic plan will also help to ensure that key ANAN leaders are following the same course. This will serve as the guidepost for the whole organization, including Council, Committees, and staff, whose activities and priorities should support overall ANAN strategic direction.

68. **Pursue vigorously the current ICAN initiative to improve the quality of audit firms to engender quality services.** Those situations where small audit firms perform bookkeeping and auditing services for the same entity do not generate reliable financial statements. Small commercial entities should be encouraged to hire accounting personnel, and small audit firms should recruit adequate numbers of competent audit professionals.

D. Financial Sector Regulators

69. **Fast-track the current joint initiative of CBN and NDIC to support the implementation of IFRS in banking sector in order to meet the mandatory IFRS adoption**

effective deadline of January 1, 2012. An invitation for submission of expression of interest by potential consultants was published on March 7, 2011. The main objective of this consultancy is to "guide the banking sector, towards a seamless and orderly implementation of IFRS in Nigeria." It seems that the gap assessment and determination of ways and means of bridging the gap would be difficult to complete in time to prepare the banks for meeting the scheduled effective date. The same consultants would also provide assistance to the supervisory personnel in CBN and NDIC to build their technical capabilities with regard to IFRS. In order to effectively implement IFRS, the banks will need to upgrade operations regarding system development, human resource development, and hardware and software procurement. The banking regulators will also need their own capacity building. In order to facilitate quick completion of preparatory work for IFRS implementation in banks, the regulators and others would benefit from drawing on the experience of IFRS implementation in some local banks during 2009-2010.

70. **Develop IFRS technical capacity in the Securities and Exchange Commission and other relevant regulatory bodies.** Immediate steps should be taken to prepare a team of IFRS experts at the Securities and Exchange Commission. These experts will be able to effectively carry out activities at the Commission, in collaboration with NASB/FRC, with regard to ensuring IFRS compliance by the quoted companies. The quoted companies in Nigeria will be required to follow IFRS when it goes into effect on January 1, 2012. In order to support activities toward making this happen, the Securities and Exchange Commission should take steps like that of the CBN/NDIC joint initiative earlier mentioned. Similar IFRS technical capacity building is necessary in NAICOM, Nigeria Stock Exchange, Federal Inland Revenue Service, and Corporate Affairs Commission.

E. Professional Education and Training

71. **Provide appropriate training and education arrangements in all parts of the country to facilitate IFRS application by corporate entities in Nigeria**. The adoption and implementation of IFRS in Nigeria will be effective if corporate entities and their auditors have been thoroughly trained in IFRS and if investors and other users of the financial statements, such as analysts and rating agencies, have been adequately brought up to date with knowledge of the practical aspects of IFRS. However, the curricula, whether in academic or professional environment, received by most accountants in Nigeria include study of Nigerian Statement of Accounting Standards but does not include IFRS similarly. Those specialists such as actuaries and valuation experts who are engaged by corporate management to assist in measuring certain assets and liabilities should undertake comprehensive IFRS training. Professional associations and industry groups should integrate IFRS into their training materials, publications, testing, and certification programs. More importantly, all colleges and universities in the country should prioritize the inclusion of IFRS in their curricula. Moreover, the curricula of professional examinations should focus prominently on IFRS requirements. Continuing professional development programs of professional accountancy organizations should include practical aspects of IFRS implementation appropriate to the Nigerian business environment.

72. **Enhance the academic and professional education and training by considering the following:**

- University-level accounting curricula should be reviewed to ensure a consistent approach is followed in Nigeria's universities. Particular focus should be given to include the practical application of IFRS and ISA, ethics, communication skills, and professional judgment to best prepare accountants (rather than bookkeepers) for careers in the corporate sector.
- The staff of regulatory agencies should have adequate exposure to practical dimensions of accounting and auditing requirements in line with international good practice. Furthermore, they should undertake industry-specific training to update their skills.
- Accountants in state-owned enterprises should be encouraged to enroll in retooling programs, and companies should also take a similar approach to support employee training and study toward professional accountancy qualification.
- The ICAN and ANAN should develop guidance on how to arrange delivery of high-quality training programs on practical implementation aspects of IFRS, ISA, and IESBA Code of Ethics for Professional Accountants.
- The ICAN and ANAN should reinforce the importance of continued professional development in order to ensure that members are fulfilling their requirement to upgrade professional knowledge. There is a clear need for improvement in the content, structure, and delivery of CPD programs.
- Corporate accountants, regulators, auditors, taxation officers, and other participants in the financial reporting process should be encouraged to seek and receive education and training for discharging their professional responsibilities effectively.