

# PDF - IMPACT OF CORPORATE GOVERNANCE ON PUBLIC CONFIDENCE IN FINANCIAL REPORTING (A CASE STUDY OF UNILEVER PLC, LAGOS STATE) - researchcub.info

## CHAPTER ONE

### INTRODUCTION

#### BACKGROUND OF THE STUDY

The preparation of stewardship report from the accounting point of view is the role of management, who oversees the affairs of the business organization on behalf of the owners usually the shareholders. This stewardship report represents the financial statements covering the operating performance and the financial position of a company. It is usually prepared by the directors and addressed to the shareholders as a fulfilment of their agency responsibility. Suffice to say that if all the facts concerning financial transactions were properly and accurately recorded, and if the owners and managers of business enterprises were entirely honest and sufficiently skilled in matters of accounting and recording, there would be little need for independent auditing. However, human nature being as it is, there probably will always be a need for the auditor to ensure the provision of dependable financial information which is essential to the very existence of our society and the business world. The goal of the providers of accounting information runs directly counter to those of the users of the information. Implicit in this line of reasoning is the recognition of the social need for independent auditors, individuals with a professional competence and integrity who can tell whether the information on which investors can rely constitutes a fair picture of what is really going on in an enterprise. Good accounting and financial reporting is the basis for society to allocate its resources in the most efficient manner. The contribution of the independent auditor is to give credibility to financial statements for this singular fact (Oyadonghan and Ibanichuka 2014). Credibility in this usage means that the financial statements can be believed; that is, they can be relied upon by outsiders, such as trade creditors, bankers, stock holders, government and other interested third parties. Therefore Credibility is "The quality of being generally accepted and trusted" (Oxford Advanced Learner's Dictionary of English). Audited financial statements are now the accepted means by which business corporations report their operating results and financial position. The word audit when applied to financial statements means that the statements of financial position, income and changes in equities /retained earnings are examined with an audit report prepared by independent public accountant, expressing a professional opinion as to the fairness of the company's financial statements. On the other hand, Confidence is the feeling that you can trust, believe in and be sure about the abilities or good qualities of something or somebody. Audit competence can only be achieved if public confidence on audit reports can be improved significantly. Both credibility and confidence goes hand in hand and each variable impacts on each other to achieve the audit quality and competence the users of financial statement desires. However, management failure arising from co-operate governance failure over the years had contributed to the loss of credibility in audit reports. The solution to this problem of credibility in financial and audit reporting lies in appointing an independent person and public confidence in audit reports is enhanced when the profession encourages high standards of performance and conduct on the part of all practitioners. According to Olagunju (2011), for an audit to be credible and reliable, it must be performed by someone, who is independent and cannot be influenced by position, power which will affect its own conclusion. Auditor independence helps to ensure quality audit (Oyadonghan and Ibanichuka, 2014). The UK financial Reporting Council (UKFRC) has undertaken an extensive reform on audit quality and in February 2008 released the audit quality framework to improve i.e. the confidence and credibility in audit. They include the culture within an audit firm, the skills and personal qualities of audit partners and staff,

the effectiveness of the audit process; the reliability and usefulness of audit reporting; and factors outside the control of an auditor that affect the audit quality (Linberg and Beck, 2011). The aim of this research work is to improve audit reliability and public confidence, by utilizing the significance of confidence and credibility as approaches to improving audit competence. One of the cumulative negative effects that window dressing (creative accounting) had was the collapse of some USA giant companies such as Enron; WorldCom, Global Crossing, Tyco, with a host of others in Nigeria (Linberg and Beck 2011). The outcome of the investigations on the collapse of these firms shows that they have been window dressing their accounts with false statements of financial positions for years. This has affected the confidence of the public on the favourable audit reports these companies had been having for the affected periods. Therefore it is good to determine what measures can contribute to improving public confidence in audit reports in Nigeria, and to establish some causes responsible for the lack of public confidence in audit report.

## 1.2 STATEMENT OF PROBLEM

Bushman et al., (2011) advanced that the information quality increases with the percentage of outside directors. Similarly, (Beekes et al., 2011) noticed that the board independence allows disclosing information of good quality by the firms in Nigeria. In other contexts, (Firth et al., 2007) indicated that the presence of independent directors improves the earnings quality of firms. In contrast, other studies suggested that the independent directors are not enough competent to control the managers and their presence in the board has no effect on the reporting quality. In addition to that, the corporate governance literature has emphasized the need to separate the positions of CEO (chief executive officer) and board chairman to guarantee the board independence and improve the firm transparency (Jensen, 1993). Byard et al., (2009) indicated that the presence of a CEO who serves also as the board chairman is associated with poor quality of financial information. Nevertheless, other authors did not detect a significant association between CEO duality and information quality in various contexts of studies (Ahmed et al., 2009; Petra 2007). (Beasley, 1996) argued that the probability of detecting financial statement fraud in the American firms decreases with the percentage of outside directors. (Peasnell et al., 2012) and (Klein, 2012) revealed that the independent board mitigates earnings management. Based on the above, this study is aiming to answer the following statement, which represents the study question: "Do Corporate Governance Practices have impact on public confidence in Financial Reporting Quality in Nigerian firms?" Poor application of corporate governance, which is considered one of the most important pillars to enhance transparency, increase control and supervision on management and reduction of fraud committed by some executives and companies Boards of Directors, which may cause damage to shareholders, investors, stakeholders, and company's reputation as well as. The purpose of this study is to investigate the impact of corporate governance on public confidence in financial reporting.

## 1.3 AIMS OF THE STUDY

The major purpose of this study is to examine the impact of corporate governance on public confidence in financial reporting. Other general objectives of the study are:

To examine the importance of financial reporting in corporate governance

To measure the effectiveness of corporate governance Code in relation to minimization of earnings management

To examine how the impact of corporate governance on public confidence in financial reporting.

To examine whether corporate governance help in building public's confidence in financial report.

To examine the relationship between corporate governance and public confidence in financial reporting.

To examine the problems of good corporate governance in a business firm.

#### 1.4 RESEARCH QUESTIONS

What is the importance of financial reporting in corporate governance?

How is the effectiveness of corporate governance Code in relation to minimization of earnings management?

What are the impacts of corporate governance on public confidence in financial reporting?

Does corporate governance help in building public's confidence in financial report?

What is the relationship between corporate governance and public confidence in financial reporting?

What are the problems of good corporate governance in a business firm?

#### 1.5 RESEARCH HYPOTHESES

Hypothesis 1

H0: There is no impact of corporate governance on public confidence in financial reporting.

H1: There is a significant impact of corporate governance on public confidence in financial reporting.

Hypothesis 2

H0: There is no significant relationship between corporate governance and public confidence in financial reporting.

H1: There is a significant relationship between corporate governance and public confidence in financial reporting.

#### 1.6 SIGNIFICANCE OF THE STUDY

The study importance stems of its attempt to highlight the importance of corporate governance and principles, in enhancing public confidence in financial reporting in business entities since these companies are deemed one of the most important sectors in of capitals attracting processes that requires enhancing their position among other sectors in Nigerian market through proving their credibility and transparency to increase shareholder trust and other parties. Geographically, the study will cover the global view on issues of public confidence and credibility in audit and financial reporting. Cases of window dressing and collapse of corporate governance as it negatively impacted on audit credibility is also covered, both in the global and Nigerian perspective. The study would serve as reference materials to other researchers who may want to carry out more research on this or related topic. The study would broaden the researcher knowledge on the subject

#### 1.7 SCOPE OF THE STUDY

The study is based on the impact of corporate governance on public confidence in financial reporting, a case study of Unilever plc, Lagos state.

#### 1.8 LIMITATION OF STUDY

Financial constraint– Insufficient fund tends to impede the efficiency of the researcher in sourcing for the relevant materials, literature or information and in the process of data collection (internet, questionnaire and interview).

Time constraint– The researcher will simultaneously engage in this study with other academic work. This consequently will cut down on the time devoted for the research work.

#### 1.8 DEFINITION OF TERMS

Corporate Governance: Is the system by which companies are directed and controlled. Boards of directors are responsible for the governance of their companies. The shareholders' role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate governance structure is in place.

**Public Confidence:** Trust bestowed by citizens based on demonstrations and expectations of: (1) Their government's ability to provide for their common defence and economic security and behave consistent with the interests of society; (2) Their critical infrastructures' ability to provide products and services at expected levels and to behave consistent with their customers' best interests.

**Financial Reporting:** Financial reporting is the process of producing statements that disclose an organization's financial status to management, investors and the government.

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