Fair Value Accounting and Earnings Quality of Listed Deposit Money Banks in Nigeria.

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ABSTRACT
The quality of reported earnings could be eroded if assets and liabilities are not reported at their fair values as such financial statements lack global comparability and consistency. The main objective of this study was to examine the effect of fair value accounting on earnings quality of listed deposit money banks in Nigeria. The study employed ex-post factor research design; the population of the study comprised 13 deposit money banks out of which 11 were purposively selected for the study. The study used secondary data, panel data regression technique was adopted in analyzing the data and the statistical package utilized for the study was SPSS version 21. The results of the analysis revealed that fair value gain or loss through profit/loss has nonsignificant effect on earnings persistence; fair value gain or loss through other comprehensive income has significant negative effect on earnings persistence and fair value intensity has significant negative effect on the earnings persistence of listed deposit money banks in Nigeria. It was concluded that fair value accounting has significant effect on earnings quality of listed deposit money banks in Nigeria. Therefore, it was recommended that management of deposit money banks should consistently follow the criteria of IFRS 9- Financial instrument and IFRS 13- Fair value measurement in classifying and measuring the elements of financial statement.

Keywords: *Fair value accounting, earnings quality, earnings persistence, fair value intensity*

1.0 INTRODUCTION

Accounting measurements and disclosures are the most important factors that affect earnings quality. In order to evaluate financial investments in a way that reflects the market value more accurately, the fair value approach is recommended over the historical cost approach. Adoption of fair value increases the quality of accounting information and helps both management and investors to assess the efficiency of maintaining a company's assets. There have been differing views when fair value accounting is compared with historical cost accounting (HCA). Some researchers argue that fair value accounting is more reliable while others state otherwise. Proponents of FVA argue that relative to historical cost accounting, FVA enhances relevance, comparability and timeliness of accounting numbers and also improve financial reporting quality (Ji, 20I9). Historical cost is said to be less reliable over time and does not have the ability to foster reliable decision once a certain period after the occurrence have passed (Pompili & Tunito, 20I9). This is because financial reports prepared using historical records of assets and liabilities lack up to date information on current values; and historical cost includes sets of assumptions and different postulates with which it is not possible to make highly accurate comparisons (Shaban et al., 2020). Thus, fair value emerged to cover these short comings resulting from the application of historical cost accounting.

According to Pompili and Tunito (20I9) assets and liabilities measured at fair values are market based inputs thereby presenting timely and relevant information. Reporting the fair values of assets in the financial statements trigger the attention of shareholders to the value of the equity and to periodic adjustment in their value as is reflected by the market mechanism that determines the prices of assets and liabilities (Shaban et al., 2020). Exposure to fair value accounting is measured using comprehensive or net income approaches. That is, changes in fair values can be reported as gains and losses through profit or loss or gains and losses through other comprehensive income. The gains and losses reported in the profit or loss sections are those realized gains or those specifically stipulated by certain accounting standards such as IAS 40 'investment properties' IAS 41 'Agriculture', IFRS 9 'Financial Instruments', and so on. On the other hand, the unrealized gains and losses such as revaluation surplus/deficit and those specifically required by certain accounting standard such as IFRS 9 are reported in the other comprehensive income. Also, fair value intensity measures the proportion of fair value assets to total assets of the company. Earnings quality refers to the extent to which the earnings figure as contained in the financial report represents the actual earnings of the firm for the period being reported. The issue of earnings quality is of great importance to market participants and the financial reporting process. Investors also pay close attention to earnings quality in order to better assess a company's value and performance and to make the right investment decisions (Fieehtar, 2021). It is worth noting that fair value accounting influence the quality of earnings because disclosures of changes in fair value as required by the IFRS reduces manipulation of reported earnings. Yao et al. (2018) predicted that fair value exposure can either increase or decrease earnings quality.

The implementation of fair value accounting over historical cost accounting particularly under the IFRS framework has introduced significant changes on how financial assets and liabilities are reported. Historical cost accounting (HCA) has failed to reflect the effect of changing price level as assets are disclosed in the statement of financial position at unrealistic values and the statement of profit or loss does not bear proper changes particularly for depreciation and cost of material consumed. This has reduced the quality of earnings reported which lack global comparability and consistency. This has been worsening as management has the discretion to choose any accounting policy whether historical cost or fair value model except for some standards that have expressly stated that certain items must be measured at fair values

Related empirical studies have been carried and some gaps were identified. From the literature, it was found out that most of the studies on fair value and earning quality were done outside Nigeria (Takacs et al. 2024; Shaban et al. 2020). In addition to the above, most researchers on fair value focused its effect on other factors such as earning management, profitability, internal control earning, earning relevance. (Abiahu et al., 2024; Etim et al., 2023; Akpan et al., 2022). This study took a step further to ascertain the effect of fair value on earnings quality. Unfortunately, there was conflicting results from previous studies as some studies established a positive effect, others negative effect while some did not even find any effect or relationship existing between those two variables. Thus, it was against this backdrop that this study was undertaken to ascertain the effect of fair value accounting on earnings quality of selected deposit money banks in Nigeria.

2. 0 LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

Theoretical framework

The major theory this study was Positive accounting theory.Positive Accounting Theory (PAT) attempts to explain why certain companies choose specific accounting choices over others. PAT assumes that incentives to management are the main determinants of accounting choices. Under the opportunistic perspective of positive accounting theory, management is expected to choose an accounting option that will meet their wealth maximization objectives. It is estimated that management will choose an income increasing choice that could positively affect their compensation and avoid the violation of debt covenants (DaiFei, 2014). PAT can be used to explain manager's choices of certain accounting methods in terms of self-interest. The choice to employ fair value accounting is discretionary in nature for level 2 and 3 valuations. The incentives for using Level 3 inputs are however constrained by the strength of the corporate governance mechanisms (DaiFei, 2014). If financial institutions are able to use the discretion available under Level 3 inputs for earnings and capital adequacy managements, the benefits of adopting IFRS will be off-set by the consequences from opportunistic behavior (DaiFei, 2014).

The positive accounting theory support this study because it assumes that incentives to management are the main determinants of accounting choices, which significantly influenced the earnings quality. This theory requires that the quality of financial reports should reflect in the ability of earnings to guide the principal in the use of his resources and in ascertaining to what extent, the management is maximizing shareholder's wealth.

Fair value accounting

According to IFRS 13, fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participant at a measurement date. As observed by Ijeoma (2014) and Akpan et al. (2022) fair value exhibit the most current and complete value estimates of financial assets and liabilities reflecting the amounts, timing, and riskiness of the future cash flows attributable to such assets or obligations. Fair value accounting is a method of measuring the value of an asset or liability based on its current market value. IFRS 13 "Fair value Measurement‟ establishes a framework for measurement of fair value and this standard was introduced by International Accounting Standard Board (IASB) in order to improve the quality of financial reporting worldwide. The financial statements prepared based on the provision of this standard is bound to show the earnings quality of the firm as earnings management would be minimized compared to the historical cost approach. As observed by Ijeoma (2014), fair value exhibit "the most current and complete" value estimates of financial assets and liabilities, reflecting the amounts, timing and riskiness of the future cash flows attributable to such assets or obligations (IFRS 13, IFRS 9, and IAS 39).

2.1.2 Earnings quality

Earnings quality refers to the extent to which the earnings figure as contained in the financial report represents the actual or fundamental earnings of the firm for the period being reported (Andrew *et al*., 2018). It also refers to the accuracy, reliability and sustainability of a company's reported earnings. The fundamental or actual earnings is that which faithfully represents the true economic performance of the firm and thus, fairly reflects the current operating performance of the firm and useful in directing forecast accuracy about the future performance and profitability of the firm (Daifei et al., 2023). The underlying idea is that the earnings report "should faithfully represent changes in wealth" (Francis et al., 2016). Prior researches on earnings quality have employed various measures as proxies of earnings quality because of different perspectives in the understanding of the construct but this study employed earnings persistence. Earnings persistence measures the extent that current earnings persist or recur in the future. High persistence is positively associated with high earnings quality, since it indicates a stable, sustainable and less volatile earnings generation process that is particularly valued by investors. Takacs et al. (2020) defined persistence as the degree to which earnings performance persists into the next periods implying that mangers have not use their discretion in the reporting processes.

Fair value gains or losses through profit/loss and earnings persistence

Generally, items whose changes in fair value are recognized in profit or loss statements are those with realizable value or those items whose changes in fair value are strictly required by their specific standards to be reported in profit or loss statements. For example, IAS 40 – 'Investment Properties' and IAS 41 – 'Agriculture' require changes in fair value and changes in biological assets (Akpan et al., 2022) to be recognized in the profit or loss statement. Since the measurement for items here are based on changes in financial assets, the study follows the procedure stipulated by IFRS 9. According to IFRS 9 financial assets are initially measured at cost and subsequent measurement depends on the business model of the enterprise and the contractual cash flow characteristics of the assets. Alves et al. (2020) found a positive relationship between fair value through profit or loss and earnings quality. Similarly, Olaoye and Ibukun-Falayi (2020) established that fair value through profit or loss positively enhances the relevance of earnings quality. Ji (2019) found that while fair value through profit or loss provides relevant information, its impact on earnings quality is mixed as it can introduce volatility and complexity in financial reporting. Thus, based on this evidence, the study hypothesized that;

H_{01}: Fair value gain or loss through profit/loss has no significant effect on earnings persistence of listed deposit money banks in Nigeria.

Fair value gain or loss through other comprehensive income (OCI) and earnings persistence

Other comprehensive incomes (OCI) are revenues, gains or losses under both Generally Accepted Accounting Principles (GAAP) and international financial reporting standards (IFRS) that were excluded from net income in the profit or loss statement but still affect equity. Revenue, gain or loss appear in other comprehensive income, when they have not yet been realized. This study used the changes in fair value of financial assets measured through other comprehensive income. According to IFRS 9 financial assets are initially measured at cost and subsequent measurement depends on the business model of the enterprise and the contractual cash flow characteristics of the assets. Financial assets whose business model is hold to collect and passed the contractual cash flow test is subsequently measured at fair value through other comprehensive income. Akpan et al. (2022) found that some major attributes influence the measurement of items under fair value through other comprehensive income. Chukwu et al. (2020) found that investors' perception of earnings quality is not associated with the fair value through other comprehensive income. Olaoye and Ibukun (2020) found that FVTOCI has significant positive relationship with earnings quality (EQ). Shaban et al. (2020) concluded that the unrealized gains or losses of fair value forecasted through comprehensive income have a high predictive power of earnings quality. Based on these findings, this study hypothesized that;

H_{02}: Fair value gains or loss through other comprehensive income does not significantly affect earnings persistence of listed deposit money banks in Nigeria.

Fair value intensity and earnings persistence

Fair value intensity refers to the extent to which a company's assets and liabilities are measured at fair value rather than historical cost. Bratten et al. (2023) conceptualized fair value intensity as the proportion of an entity's assets that is fair valued (total fair valued assets/total assets) and included or disclosed in the financial statement. Following Etim et al. (2023), they measured banks fair value accounting exposure as the summation of assets and liabilities recognized at fair value scaled by total assets. Daifei et al. (2023) tested the usefulness of fair values in improving the predictive ability of earnings from a sample of two hundred non-US bank from twenty four countries between 2019 -2022. They utilized regression and documented that more fair values on balance-sheet financial instruments enhances the ability of current earnings to predict future earnings and cash flow. Horsfall and Omah (2023) examined the effect of economic consequences of adopting fair value accounting under IFRS, including how fair value intensity affects earnings quality in Jordanian banks. The findings revealed that high fair value intensity can increase earnings volatility due to fluctuations in market values. Yao et al. (2018) investigated how fair value intensity affects earnings quality in Nigerian banks, and found that the use of fair value can enhance the relevance of financial statements by providing timely information. Etim et al. (2023) found a positive association between Fair value intensity and earnings management Thus, based on this evidence, this study hypothesized that;

H_{02}: Fair value intensity does not have significant effect on earnings persistence of listed deposit money banks in Nigeria.

3.0 METHODOLOGY

This study adopted ex-post facto research design in ascertaining the effect of fair value accounting on earnings quality of listed deposit money banks in Nigeria. This design was suitable for this study because the study made use of secondary data that were extracted from the studied banks' annual reports. The population of this study consisted of thirteen (13) listed deposit money banks in Nigeria. The study employed a purposive sampling technique to select 11 deposit money banks listed on the Nigerian Exchange Group (NGX) as of December 31, 2023. The inclusion criteria required banks to have financial statements presented in Nigerian currency, operate as interest-based institutions, and provide comprehensive annual reports over the study period. The data were analyzed using panel regression technique and the statistical package employed was SPSS version 21.

Model specification

The functional model for this study was adopted from the work of Takacs et al. (2020) and modified to suit this study as stated below;

Earnings quality = f(fair value accounting)

Earnings persistence =f(fair value through profit and other comprehensive income, fair value through profit or loss, fair value intensity)

$PESIS_{it} = \alpha_0 + \beta_1 FVTPI_{it} + \beta_2 FVOCI_{it} + \beta_3 FVINT_{it} + \varepsilon_{it}$

Where:

PESIS	=	Earnings persistence
FVTPL	=	Fair value gains or loss through profit or loss
FVOCI	=	Fair value gains or loss through other comprehensive income
FVINT	=	Fair value intensity
β_0	=	Model intercept
β_{1-3}	=	Coefficient to be estimated
it	=	Cross section of listed deposit money banks with time variant
ε_{it}	=	Stochastic error term

Measurement and operationalization of variables

Variable	Measurement	Sources	Apriori expectation
Earnings persistence (Dependent variable)	Log of standard deviation of the earnings of the sampled banks. Low variations signal high earnings persistence.	Takacs et al. (2020)	
Fair value gains or loss through profit or loss (Independent variable)	Log of fair value gains or loss through profit or loss as presented in the sampled banks' annual reports.	Chukwu et al. (2020)	+ve
Fair value gains or loss through other comprehensive income (Independent variable)	Log of fair value gains or loss through other comprehensive income as presented in the annual reports of the sampled banks.	Chukwu et al. (2020)	+ve
Fair value intensity (Independent variable)	Total fair valued assets divided by total assets.	Bratten et al. (2023)	+ve

Source: Author's operationalization (2025)

4.0 RESULT AND DISCUSSION

Descriptive statistics of the variables

Table 4.1 Descriptive statistics of the fair value accounting and earnings quality of listed deposit money banks in Nigeria

	N	Minimum	Maximum	Mean	Std. Deviation
pesis	110	1,333,721	56,4000,000	10,580,718	11,624,215
fvtpl	110	-33403225	3355460000	100736126.52	394232939.21
fvoci	1110	-58130977	398305000	9354213.00	43309465.29
fvint	110	.0000	.5046	.105635	.0987184
Valid N (listwise)	110				

Source: Researcher's computation (2025)

Table 4.1 shows the descriptive statistics of all variables under study. From the table, it was observed that earnings persistence in banking sector was on the high side, this was evident as the minimum was ₦1,333,721, maximum was ₦56,400,000 average was ₦10,580,718,with standard deviation of ₦11,624,215. Low level of variability was also present in the earnings persistence of the sampled banks. Fair value gain or loss through profit or loss (fvtpl), it was observed that the average bank gains about N100,736,126.52 with a standard deviation of N394,232,939.21 indicating normal level of variability in these values. Fair value gain or loss through profit or loss in the banking sector between 2014 and 2023 ranged from -N33, 403,225 to N3, 355,460,000. This indicator was very high in the banking sector. From the table too, fair value gain or loss through other comprehensive income (fvoci) showed a maximum value of N398,305,000 and an average of N9,354,213. However, the minimum was -N58,130,977 with standard deviation of N43,309,465.29 which showed very high level of variability in the data. With the very high standard deviation, it can be said that this metric was relatively low in the banking sector. Lastly, for fair value intensity, the average bank had about 11% of total assets to be fair value assets. This was with a standard deviation of about 10%. Already, these entail lack of variability in this particular data. This means that fair value intensity from bank to bank was not significantly different. However, these percentages ranged between 0 and 50 according to table 4.1.

Table 4.2 Normality test

	Kolmogorov-Smirnov[a]			Shapiro-Wilk		
	Statistic	df	Sig.	Statistic	df	Sig.
Pesis	.202	109	.000	.922	109	.009
fvtpl	.134	109	.070	.858	109	.000
fvoci	.195	109	.001	.697	109	.000
fvint	.190	109	.001	.884	109	.001

a. Lilliefors Significance Correction
Source: Researcher's computation (2025)

From table 4.2 above, it was observed that none of the study variables followed a normal distribution as all p values were less than 0.05 level of significance and so, all null hypotheses were rejected. However, the study proceeded with the Ordinary least square regression analysis but depending on the probability statistics against the t-statistics for interpretation and policy recommendation as suggested by Greene (2009).

Table 4.3 Correlation analysis for fair value accounting and earnings quality of listed deposit money banks in Nigeria

	pesis	fvtpl	fvoci	fvint
pesis	1.000			
fvtpl	.184	1.000		
fvoci	-.206	.415	1.000	
fvint	-.064	.045	.084	1.000

Source: Researcher's computation (2025)

From table 4.3 above, the correlation results show that; each of the variable have a perfect correlation with themselves with a coefficient of 1.000. Reporting further, fair value gain or loss through profit or loss (fvtpl) had weak negative correlation (0.184) with earnings persistence (pesis). This implies that increase in fvtpl usually comes with high standard deviation of earnings to a low extent. Secondly, fair value gain or loss from other comprehensive income had a weak negative correlation with standard deviation of earnings of the sampled banks (-0.206), and lastly, fair value intensity (fvint) had no correlation with standard deviation of earnings persistence (pesis) (-0.064) in the sampled banks.

Regression analysis

Table 4.4 Model summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.654[a]	.428	.411	.079552838	1.564

a. Predictors: (Constant), fvoci, fvint, fvtpl

b. Dependent Variable: pesis

Source: Researcher's computation (2025)

Table 4.5 Analysis of variance (ANOVA)

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	.317	3	.002	8.349	.000[b]
	Residual	.228	106	.006		
	Total	.544	109			

a. Dependent Variable: pesis

b. Predictors: (Constant), fvoci, fvint, fvtpl

Source: Researcher's computation (2025)

Table 4.6 Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	2.726	.185		14.733	.000		
	fvint	-.116	.197	-.100	-2.892	.009	.942	1.062
	fvtpl	.093	.121	.135	.765	.449	.869	1.150
	fvoci	-.171	.153	-.184	-3.463	.006	.828	1.208

a. Dependent Variable: pesis

Source: Researcher's computation (2025)

The regression outputs presented above showed an F-statistic of 8.349 with p-value of 0.000 indicating that overall, the model is fit for statistical inference and also that overall, the relationship between fair value accounting and earnings persistence is statistically significant. The model gave an R-squared value of 0.428 which means that 42.8% of the changes in earnings persistence could be explained by the proxies of fair value accounting in the model. However, the unexplained part (57.2%) was captured in the error term.

Discussion

Fair value gain or loss through other comprehensive income and earnings quality

Results from the pooled OLS regression model showed that fair value gains through other comprehensive income (fvoci) with coefficient and p-value of -0.184 and 0.006 respectively, has a significant negative effect on the standard deviation of earnings. It was noted in the variable measurement that the lower the deviation, the higher the quality (persistence). This therefore means that fair value gain or loss through other comprehensive income could enhance earnings persistence of listed deposit money banks in Nigeria. This could be attributed to enhanced transparency and predictability in financial reporting. FVOCI reflects fair value adjustments recognized in other comprehensive income rather than profit or loss, thereby reducing volatility in reported earnings. This stability enhances the predictability of earnings, a critical aspect of earnings persistence, making financial information more reliable for stakeholders. The finding is in line with Abiahu, et al. (2024) who was of the view that the primary effect of FVOCI is the reduction in earnings volatility, adding that since changes in the fair value of FVOCI instruments are recorded in OCI rather than profit or loss, the effect of these fluctuations on reported earnings is mitigated.

Fair value gain or loss through profit or loss and earnings quality

Output of the OLS model in table 4.6 presented 0.135 and 0.449 as coefficient and p-value respectively. It is evident that the p-value was insignificant at the 5% level. This indicates that fair value gain or loss through profit or loss has non significant effect on earnings persistence of listed deposit money banks in Nigeria. The nonsignificant effect of fair value gains or losses through profit or loss (FVTPL) on earnings persistence may be explained by the inherent volatility and short-term focus associated with such measurements. FVTPL requires immediate recognition of fair value changes in the income statement, which can introduce fluctuations that obscure the underlying performance of the firm. This volatility may undermine the stability and persistence of earnings, making it difficult for stakeholders to rely on such figures as an indicator of long-term earnings quality. Additionally, the nature of items classified under FVTPL often involves financial instruments held for trading or speculative purposes. These instruments are more susceptible to market fluctuations, and their impact on earnings may not reflect the bank's core operational performance. As a result, stakeholders may discount their influence when assessing the overall quality and persistence of earnings. This finding is contrary to the findings of Shaban et al. (2020) and Olaoye and Ibukun (2020) who all showed significant relationship in their contexts.

Fair value intensity and earnings quality

From table 4.6, it was also observed that a coefficient of -0.100 and a corresponding p-value of 0.009 was the case, implying that fair value intensity has a significant negative effect on the standard deviation of earnings of listed deposit money banks in Nigeria. This in turn implies that fair value intensity has a significant positive effect on earnings persistence (persistence). This means that increase in fair value intensity causes increase in earnings quality of listed deposit money banks in Nigeria. This outcome implies that an increased reliance on fair value measurements in asset valuation contributes positively to the stability and reliability of earnings. By providing a more accurate and timely reflection of an entity's financial position, fair value measurements enable stakeholders to better predict future earnings, thereby enhancing their persistence. The reduction in earnings volatility may be attributed to the comprehensive nature of fair value accounting, which captures changes in asset values that are directly influenced by market conditions, minimizing the likelihood of sudden, unanticipated adjustments. This finding is contrary to Takacs et al. (2020) who revealed that high value intensity can increase earnings volatility due to fluctuations in market values. The finding is also contrary to Daifei et al. (2023) who concluded that while fair value measurements can provide a more current and transparent view of financial positions, they can also introduce "noise" into earnings if market conditions are volatile.

5.0 CONCLUSION AND RECOMMENDATIONS

This study examined the effect of fair value accounting on the earnings quality of listed deposit money banks in Nigeria, focusing on fair value gains or losses through other comprehensive income, gains or losses through profit or loss, and fair value intensity. The findings revealed that fair value gains or losses through other comprehensive income

significantly enhance earnings quality by improving earnings persistence, while gains or losses through profit or loss showed no significant effect. Additionally, fair value intensity was found to positively impact earnings quality by stabilizing earnings and reducing volatility. Based on this, it was concluded that fair value accounting has significant effect on earnings quality of listed deposit money banks in Nigeria. It was therefore recommended among others that management of deposit money banks should consistently follow the criteria of IFRS 9-Financial instrument and IFRS 13- Fair value measurement in classifying and measuring the elements of financial statement. Banks were encouraged to increase the proportion of assets valued using fair value accounting, as higher fair value intensity positively influences earnings persistence by reducing earnings variability.

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