AN ANALYSIS OF THE FRC RULES

The Financial Reporting Council of Nigeria (FRCN) acting within its powers in accordance with Section 8(2), Section 30 and Section 53(2) of the Financial Reporting Act, No.6, 2011 (“the FRC Act”) recently issued a new set of Rules on varying issues including membership of the Audit Committee and the competence of foreign audit/accounting firms to sign off on the financial statements of Nigerian Companies. The Rules are premised on the existing provisions of the FRC Act, and have been issued to give effect to the provisions of the Act.

RULE ONE- CERTIFICATION OF DOCUMENTS OF FINAL NATURE

To give effect to the provisions of Section 7 (2g) of the FRC, “persons holding the positions of CEO and CFO of an entity are required to certify the annual reports, financial statements, accounts, financial report, returns and other documents of a financial nature indicating their Financial Reporting Council (FRC) registration numbers”. The Rule also provides that “the CFO providing certification shall be a professional member of an accounting body established by Act of National Assembly in Nigeria”.

This provision is not dissimilar to Section 34.2 of the Securities and Exchange Commission (SEC) Code of Corporate Governance which provides that “the CEO and the Head of Finance Function of every public company should in a written statement to the Board certify that the financial statements present a true and fair view of the affairs of the company”.

RULE TWO- PROFESSIONAL CERTIFICATION AND EXPERT OPINION

This Rule relates to assurance opinion expressed by professionals engaged in the financial reporting process relating to financial statements, accounts, financial reports, returns and other documents of a financial nature. The rule defines a professional for the purpose of FRC registration “as any person whose judgement can be relied upon due to his education or training, and who possesses certification issued by a recognised professional body or association and is currently working or wishing to work in Nigeria”.

The Rule provides further that “any person attesting, as Chairman of Audit Committee, to annual report[s], financial statements, accounts, financial report, returns and other documents of a financial nature, shall be a professional member of an accounting body established by Act of National Assembly in Nigeria”.

This Rule takes into cognisance the fact that professional/expert opinion on financial statements and accounts may be required on any portion of the accounts, and can be given by any professional in any field. In view of this, the FRC Act makes it mandatory for all professionals to register with the FRC, and for the FRC registration number of such professional to be included in the financial statements and accounts.
We note that this Rule has failed to give due recognition to the rigorous accreditation undertaken by different professional bodies in Nigeria. For instance, to practise as a lawyer in Nigeria, the individual is expected to have a law degree, obtain a BL from the Nigerian Law School, and must have been called to the Nigerian Bar. Requiring a legal practitioner to procure registration with the FRC gives an indication that the certificate issued by the Council of Legal Education and membership of the Nigerian Bar Association have no credibility whatsoever.

RULE 3 - AUDITOR INDEPENDENCE

This Rule provides for the disclosure of audit fees paid by an entity to its External Auditors, non-audit services rendered by the External Auditor and the fees paid thereon., The rule is largely in sync with the provisions of the Companies and Allied Matters Act and seeks to promote auditor independence.

The Rule takes due cognizance of the difficulty involved in conclusively drawing up a list of situations where provision of non-audit services to an audit client could create threats to independence and objectivity of the external auditor, and provides that “where an audit firm and/or its related entity offers non-audit service(s) to an audit client, the audit client shall disclose the details of such non-audit services and the applicable fees paid thereon in the notes to its financial statements”.

The Engagement Partner is also required to ensure that the non-audit service(s) are not prohibited and pose no threat to the audit firm’s independence and objectivity.

RULE 4 - REGISTRABLE TRANSACTIONS

The fourth Rule provides that all transactions or events of any financial nature requiring registration or approval of any statutory or regulatory authority in Nigeria (e.g. the National Office for Technology Acquisition and Promotion [NOTAP]), shall only be considered as having financial reporting implications when such registration or approval is obtained. The Rule provides further that it is not sufficient to obtain the registration as required by law, details of the registration (including but not limited to the registration certificate number, approved amount, approval basis, validity period and subject matter) must also be disclosed in the note to the financial statements if the transaction is recognised as part of the financial reporting of the entity.

The Rule also requires the disclosure of the financial implications of inter-company transfer and technical management agreements between the company and its significant local and overseas suppliers (if any).

RULE 5 - SUBMISSION OF FINANCIAL STATEMENTS FOR WHICH EXTERNAL AUDITORS EXPRESSED QUALIFIED OPINION

This reiterates Section 8(1) (n) of the FRC Act No. 6 of 2011 which provides that the FRC shall “receive copies of all qualified reports together with detailed explanations for such qualifications from auditors of the financial statements within a period of 30 days
from the date of such qualification and such reports shall not be announced to the public until all accounting issues relating to the reports are resolved by the Council”.

The Rule defines qualified report as “all reports (including emphasis of matter, qualified, adverse, disclaimer, etc.) other than unqualified reports issued by External Auditors on an annual report, financial statements, accounts, financial report, returns and other documents of a financial nature”.

RULE 6- NON-SUBMISSION OF FINANCIAL STATEMENTS WITHIN STIPULATED TIME

Like Rule 5, Rule 6 merely re-states the provisions of Section 8 (1) (d) which require public interest entities to submit their financial statements to the Council within 60 days of approval of such financials statements by the Board of the Public Interest Entities in line with the requirements of Section 8(1)(d) of the FRC Act. It also reiterates the provisions of Section 58(3) of the FRC Act which provides that “Where a public interest entity files any financial statements and report with any government department or authority, the entity shall also file a copy of the financial statements and reports with the Council within 30 days, in such manner as may be set out in the rules of the Council”.

Entities in breach of this Rule shall be liable to civil, administrative and criminal sanctions as provided under the FRC Act.

We note similar compliance requirements by other regulators. The Bank and Other Financial Institution Act requires Banks to submit their accounts to the CBN and publish the said accounts within 4 months after the end of the financial year. In the same vein, the Companies and Allied Matters Act requires the submission of Audited Accounts when filing the Annual Returns. The SEC and Nigerian Stock Exchange (NSE) also require listed entities to submit their quarterly, half-yearly and annual accounts.

There is a need for the FRC to sync compliance requirements in this regard with similar requirements by other regulators to ease the compliance burden on regulated entities.

RULE 7- OTHER NATIONAL DISCLOSURES

This Rule requires the inclusion in Financial Statements of Statements of Value Added and Five-Year Financial Summary as supplementary information and classified as “Other National Disclosures”.

RULE 8 - FUNCTIONAL AND PRESENTATION CURRENCIES

This Rule addresses the issue of the currency in which financial statements are presented, and distinguishes between functional currency and presentation currency. The Rule defines functional currency as “the currency of the primary economic environment in which an entity operates” and provides that the determination of functional currency is as prescribed in the principles contained in IAS 21 paragraphs 9 to 14 and not subject to accounting choice.

On the other hand, presentation currency according to the Rule is “the currency in which the financial statements are presented”. Unlike functional currency, the determination of
presentation currency is a matter of accounting choice as an entity may present its financial statements in any currency other than its functional currency.

The rule takes due notice of exceptional situations where companies operating in Nigeria (Oil & Gas Companies and other multinationals) are likely to have functional currencies other than the Naira, and thus draws attention to IAS 21 which is intended to provide guidance on how to translate financial statements prepared using functional currency other than the Naira, into presentation currency.

The Rule highlights the provisions of Section 8 (p) of the FRC Act which empower the Council to “specify in the accounting and financial reporting standards, the minimum requirements for recognition, measurement, presentation and disclosures in annual financial statements, group annual financial statements or other financial reports which every public interest entity shall comply with in the preparation of financial statements and reports”.

The Rule provides emphatically that the presentation currency for all general purpose financial statements in Nigeria is the Nigerian Naira. General purpose financial statements according to the Rule include “statements filed for all statutory purposes and those presented to directors, shareholders, creditors and all other stakeholders”.

The Rule gives a regulated entity the option of including an annexure to the financial statements stating the various accounts in its functional currency, where it believes that its stakeholders would be better informed by a representation of the accounts/reports in the entity’s functional currency. The entity would however be required to disclose the exchange rates applied in translating its assets, liabilities, income and expenses.

Whilst it is laudable that the FRC seeks to strengthen financial reporting regulations in its bid to protect the investing public and ensure that accurate information that present a true and fair view of the financial position of regulated entities are available, consideration should be given to the fact that most public companies who are subject of these Rules are also regulated by at least one other regulator with stringent compliance requirements. It is also worthy of note that compliance with the various regulations comes at significant cost to the regulated entities – as does non-compliance.

In view of the foregoing, and given Nigeria’s low ranking in the World Bank’s Ease of Doing Business Index, it is imperative for the FRC to work closely with other regulators to synchronize compliance requirements in order to avoid duplicity. One way of achieving this is to create a common portal where all compliance documentation agreed upon by the core regulators and the FRC would be uploaded by regulated entities, with the FRC and other core regulators having access to same.