Malaysian Management Journal Vol. 22, December 2018 19-34

RELATED PARTY TRANSACTIONS, OFF BALANCE SHEET ITEMS AND EARNINGS QUALITY OF LISTED DEPOSIT MONEY BANKS IN NIGERIA

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Abstract

This paper examines the impact of related party transactions, off balance sheet items on earnings quality of listed deposit money banks in Nigeria over the period of 4 years (2011 to 2014). Data were collected from annual reports of the sampled banks. Descriptive statistics and correlation analysis were employed, and Ordinary least square (OLS) robust regression technique was used as a tool of analysis using panel data. The study reveals that related party transactions are positively and significantly related to earnings quality. On the contrary, off balance sheet items were found to be negatively and insignificantly related to earnings quality. Based on the findings, the study concluded that related party transactions have significant impact on the earnings quality of the Nigeria deposit money bank. The study recommends that Management of the Nigeria money deposit banks should be more aggressive towards the number of genuine related party transactions that can add value to their firms when making financial decision because it is likely to have positive effects on the quality of their earnings.

Keywords: *Earnings quality, Off-balance sheet engagement, Related parties transactions, Deposit money banks*

Received: 1/11/2017 **Revised**: 19/2/2018 **Accepted**: 18/7/2018 **Published:** 14/7/2019

Introduction

Recent corporate financial scandals create an enormous challenge and weaknesses in corporate reporting around the world. A record of companies associated with financial scandals in the past decade was been reported by Badawi (2008) while Ge, Drury, Fortin, Liu and Tsang (2010) reported that scandals in the United States, such as Adelphia & the Riga family's corporate group, and Hollinger & Conrad Black's corporate group, have brought related party transactions to attract the attention of researchers and policy makers. Furthermore, corporate scandals such as Enron and WorldCom show how related party transactions and off-balance sheet engagements may reduce the reliability of reported earnings. In Nigeria Okolie (2014) reported corporate scandals including the cases of Cadbury Nigeria

Plc and African Petroleum (AP); Savannah Bank and African International Bank; Wema Bank, Nampak, Finbank and Spring Bank; and recently Intercontinental Bank Plc., Bank PHB; Oceanic Bank Plc. and AfriBank Plc. According to Okolie (2014) the above-mentioned are recognized publicly reported cases that resulted to poor earnings quality. These widespread reoccurrence of corporate financial crisis provides a need to investigate the relationship between related party transactions, off-balance sheet engagements and quality of accounting earnings, which have been observed to rise over time following the periodical business failures, frauds and court cases.

Narrowing the issues to the Nigerian the banking sector, some of the recurring areas of concerns between 2010 and 2015 were related party transactions (RPT) and off balance sheet engagements (OBSE). The use of OBSE mainly in the form of Banker's Acceptance (BA's) and Commercial Papers (CPs) by Nigerian banks in 2009/2010 led the Nigerian Central Bank (CBN) to suspend the use of CPs and BAs as financial instruments and OBSE in Nigeria. In the CBN's 2009/2010 "Special/Target Examination" of Nigerian banks, the Apex bank discovered that in an effort to hide their toxic assets from the regulatory scrutiny of the CBN, some Nigerian banks had restructured their non-performing loans into CPs and BAs and sold them to other organizations. Therefore the CBN via its Circular BSD/DIR/GEN/CIR/03/018 of July 23, 2009 suspended the use of Bas and CPs as OBSE (Central Bank of Nigeria (CBN), 2009). Although the suspension was lifted by the CBN in 2010, to control the unhealthy use of OBSE to conceal bad loans the CBN mandated the Deposit Money Banks (DMBs) to register every BA or CP booked. This was reiterated in the CBN's letter to DMBs number DSB/DIR/GEN/LAB/09/035 of July 11, 2016. Evidently in the Nigerian context, OBSE has continued to be used as a tool of managing the quality of reported earnings by DMBs in Nigeria.

On the other hand, RPT in terms of lending to related organizations or individuals have been found to be prevalent during the same period as when the banks were using OBSE to conceal toxic loans. The adoption of the universal banking system by Nigeria in 2005/2006 made it easy for most of the large DMBs to venture into providing other financial services including insurance and underwriting, discount house, registers, stock broking etcetera beyond banking services. The era of universal banking ushered in a period of significant increase in DMBs creating a complex strings RPTs in the Nigeria sector which was observed to have contributed to number of bad loans that most banks tried concealing using OBSE. This led the CBN in its "Revised Guidelines for Finance Companies in Nigeria" of April 2014, to mandate all finance companies to publicly disclose all RPTs on their website. After the Special/ Target Examination of DMBs by the CBN and reclassification (proper classification) of much of the DMBs assets, most of the banks had to recognize provisions over and above their previously declared earnings. Thus the quality of earnings reported by Nigerian DMBs in the face of RPT and OBSE remains a thing of concern to various stakeholders.

Earnings quality refers to the overall reasonableness of reported earnings. Quite often a shadow of doubt is cast around the quality and reliability of earnings reported by firms given that a good number of the recent corporate financial scandals were not predicated by poor financial performance. Particularly most of the cases recorded in the Nigerian banking sector in 2009/2010 came after the banks had reported good corporate earnings in previous accounting period before the scandal. Munir, Saleh, Jaffar, and Yatim (2013) described earnings quality as when managers do not manipulate accounting transactions and financial figures. The earnings reported by firms would reflect the true performance of the firm because the earnings are the products of genuine business transactions and calculations. Firm earnings also show the extent to which a firm has engaged in value-added activities during the course of its operational year and are signals that helps direct resource allocation in capital markets (Yero, 2011). It is widely accepted amongst scholars that value of a company's stock is the present value of its future earnings. Increase in earnings represents an increase in company's value, while decrease earnings signal a decrease in that value. Gaio and Raposo (2011) found the existence of relationship between firm valuation and an aggregate earnings quality measure based on seven earnings attributes among which value relevance is included. High quality of reported earnings indicates low levels of earnings management in the firm, or earnings that reflect the true performance of the firm (Munir et al., 2013).

Tunneling and propping are common behavior by controlling shareholders in transactions within a group structured firm. Tunneling refers to transfer of resources from a lower-level firm to a higher-level firm within the pyramidal chain while propping is concerned with transfer in the opposite direction intended to bail out the receiving firm from bankruptcy especially during bad economic times (Riyanto & Toolsema, 2008). So RPTs generally occur in a situation where a business arrangement between two parties who are joined by a special business relationship prior to the deal have been identified to have value implications for the firms involved but most importantly for the parties involved. In firms, concentrated insider ownership tends to enjoy control privileges and the opportunities to expropriate outside minority (smaller) shareholders through the firm's operating and financial decisions (Elhelaly, 2014). The expropriation of minority shareholders could be in the form of outright theft, selling assets or products at lower (higher) than market price to (from) a firm in which the controlling shareholders have a high stake (Peng, Wei, & Yang, 2011). In the banking sector, lending to related parties at less than market rate, unsecured with little or no rigorous credit risk assessment is not unheard of. Generally, poor assets quality has far reaching implication for the value of the firm and quality of its reported earnings. Quite often, risk assets created through RPTs are substandard and more likely to go bad and result in the need to manipulate earnings among managers.

On the other hand, off balance sheet items are contingent assets or liabilities that do not appear on a company's balance sheet, this is because the company does not have legal claim or responsibility for such items. Off balance sheet items are often used by firms (especially banks) to provide financing, liquidity, market or credit risk support or to engage in leasing, research and development services (Securities and Exchange Commission (SEC), 2002). The SEC (2000) also went ahead to outline the uses of off balance sheet items to some companies such as, for financing at a lower cost of capital than otherwise would be available to a company; to allocate risks among third parties. Off balance sheet financing is one of the most common ways of financing a business (Jabbarzdeh, Morteza & Mohammad, 2012). According to the proposed rule of U.S. Securities and Exchange Commission (2002), off balance sheet arrangements may involve the use of complex structures, including structured finance or special purpose entities, to facilitate a company's transfer of, or access to, assets. In many cases, the transferor of assets has some continuing involvement with the transferred assets that may assume different forms, such as financial guarantees, retained interests, keep well agreements or other contingent arrangements designed to reduce risks to the special purpose entities or other third parties. Given its nature, OBSE can be used by banks to manage their reported earnings or even to circumvent regulatory obligations such as breaching the thresh-hold for single obligor lending limits or even liquidity by guaranteeing third party loans in favour of customer that they are already exposed to.

The Nigeria banking financial crisis highlighted weaknesses in corporate governance, reporting and accounting disclosures (CBN, 2009). Some of the recurring areas of concern include the quality of the reported earnings which could be linked to the widespread use of related party transactions and off balance sheet items by Nigerian banks. Also, both RPT and OBSE are linked together, through securitization. Securitization refers to the process of transforming financial assets into securities. RPT have been directly associated with several cases of financial scandals, fraud and declined earnings quality (Elhelaly, 2014). The banking sector was chosen for the study because in the past it used to be the single most capitalised sector on the Nigerian Stock Exchange (NSE) (Oteh, 2015). Nigerian DMBs have however lost that position after the market crash of 2009/10 currently banking stocks represent account for over 70% of capitalization within the financial services segment of the market which represents about 30% of the entire market capitalization (Oteh, 2015).

The extant literature is replete with empirical studies conducted particularly in the developed and developing countries on the relationship between RPT and earning quality (Cheung, Rau & Stouraitis 2006; Cheung, Jing, Lu, Rau & Stouraitis 2009; Aharony, Lalang & Yuan 2010; Ge, Drury, Fortin, Liu & Tsang 2010; Tsai, Chang & Chang 2015; Munir, Saleh, Jaffar & Yatim 2013; Huang & Liu 2010; Pozzoli & Venuti 2014; Elhelaly 2014; Wang & Yuan 2012; Kuan, Tower, Rusmin & Zahn nd; and Gordon & Henry 2005). Other studies have documented evidence on the impact of OBSEs on earnings in both the developed and developing countries (Lozano – Vivas & Pasicuras nd; Aktan, Chan, Zikovic & Evri-Mandaci 2013; Ge 2006; Irving & Smith 2014; Lepetit, Nys, Rous & Tarazi 2006; and De young & Roland 2001). Although many studies have been conducted around the world, we could not trace any study that was focused documenting evidence on the effect of OBSE and RPT on earnings quality in the Nigerian banking sector. The findings of most of the extant studies may be limited in application in the Nigerian context given differences in economic environment (Gordon & Henry, 2005). The impetus for this study is informed by dearth of empirical studies in the Nigerian banking industry despites the number of banking crisis in its recent past and the seeming role that OBSE and RPT seemingly played impairing the quality of reported earnings by Nigerian DMBs. Based on the foregoing, this study is focused on examining the impact of RPT and OBSE on the earnings quality of listed deposit money banks in Nigeria. The reminder of this paper is structured as follows; the review of the literature which surrounds related party transactions and earnings quality, off balance sheet items and earnings quality, and theory underpinning the study; the research methodology; analysis and discussion of results; conclusion and recommendation.

Empirical Literature Review and Hypotheses Development

Earnings Quality and Related Party Transactions

The results of studies on relationship between related party transactions and earnings quality are inconclusive. Regarding related party transactions Cheung, Rau and Stouraitis (2006), conducted a study on tunneling, propping and expropriation in Hong Kong. Secondary data from published annual reports covering the period 1998-2000 were obtained and analysed using both univariate and multivariate generalized linear model. Abnormal returns were used as dependent variable to proxy earnings quality, while ownership structure, corporate governance and information disclosure as the independent variables. The results revealed that on average, firms that announce connected transactions earns significant negative excess return; on the other hand firm announcing similar arm's length transaction earns significantly lower (negative) excess return.

To link RPT to the earnings quality of reported earnings, some studies have used return on assets as a measure of earnings quality. Aharony, Wang, and Yuan (2010), investigated tunneling as an incentive for earnings management during the IPO process in China. Data from 185 Chinese IPO firms' annual reports were obtained from listed firms on the Shanghai stock exchange during the period 1999-2001 and analysed using multiple regression model. Using ROA as dependent variable, while related party sales and related party purchases as the independent variables. The result revealed that RP sales of goods and services could be used opportunistically to manage earnings upward in the pre-IPO period; such behavior may be motivated by the prospect of tunneling opportunities in the post-IPO period.

But in more recent studies, the use of discretionary accruals to measure earnings quality has become even more prevalent. Kuan, Tower, Rusmin, and Zahn (nd), examined the impact of related party transactions on earnings management. Secondary data were collected from annual reports of Indonesian public listed companies for the periods ending 2004-2005. The authors used discretionary accruals as dependent variable, while lagged total amount of related party transactions as the independent variables; the study employed OLS multiple regression model. The result revealed that there is no statistically significant evidence of the association between related party transactions and earnings management.

Similarly, Gordon and Henry (2005) investigated the impact of related party transactions on earnings management. Firm data were obtained from COMPUSTAT for the periods 2000-2001 and analysed using regression technique. They used adjusted abnormal accruals as dependent variable, while related party transactions as the independent variable. The result revealed that there is a positive and significant relation between the adjusted abnormal accruals and limited types of transactions such as fixed-rate financing from related party. Overall, it appears that concerns about related party transactions as a factor associated with earnings management are warranted, but only for certain related party transactions.

However, other studies have linked the use of RPT to corporate governance on how it affects earnings quality. Furthermore, they explain the use of RPT from the purview of tunneling and or propping of financial benefits by controlling shareholders. Cheung, Jing, Lu, Rau and Stouraitis (2009), investigated Tunneling and Propping using related party transaction by Chinese listed companies. Data were obtained from Chinese publicly listed firms for the period 2001–2002 and were analysed using multiple regression technique. They investigated the effects of corporate governance and information disclosure on firms' performance as a proxy for earnings quality. The result of the study revealed that related party transactions representing tunneling are accompanied by significantly less information disclosure compared to related party transactions representing propping. Propped up firms tends to have worse operating performance in the fiscal year preceding the announcement of related party transactions.

Similarly, Tsai, Chang and Chang (2015), examined the relationship between related party transactions and corporate value. Secondary data from annual reports were obtained from firms listed on the Taiwan stock exchange and in the Gre Tai securities market in Taiwan during the period 2006– 2012. They used book value of debt and market value of equity to total assets as dependent variables while absolute value of RPT, RPT dummy and Affiliation of the business groups as independent variables. The result revealed that both of the related party sales and purchases increase value of the affiliated firms. The institutional perspective is supported and business group affiliated firms seem to be propped up. However, when the related party sales of the affiliated firms are bigger than their related party purchase, the firm value of the affiliated firm is more likely to be lower than those of non-affiliated firms and demonstrates the tunneling motivation related party transactions.

Some other studies focus on tunneling and propping but looking at their role of family owned firms. Munir, Saleh, Jaffar and Yatim (2013), conducted a study on family ownership, related party transactions and earnings quality. They employed regression analysis while data was collected from listed firms' Malaysia for the period 2004. They examined the effect of family shareholdings and related party transaction as the independent on earnings quality of the sampled firms. The result of the study revealed that at a low level of family ownership, the positive effect of familial value are likely to outweigh the negative effects of related party transactions, however in the presence of a high level of family ownership the negative effect of related party transactions are likely to be more substantial and reduce the benefits of familial value. Also shows that there is no linear relationship between family ownership and earnings quality after accounting for related party transactions. This finding suggests that certain firms are likely to report high earnings quality if they have small level of family ownership despite low level investor protection in Malaysia. When a family has a significant ownership stake in a firm, expropriation activities appears to negatively affect earnings quality of the firm.

Whereas, others studies like Ge, Drury, Fortin, Liu and Tsang (2010), investigated value relevance of disclosed related party transactions in manufacturing firms. Secondary data from annual reports were obtained from 52 manufacturing industries listed in the "2002 Ranking" of New youth fortune, a Chinese financial Magazine during the period 1997–2003. Using price level as dependent variable while sales of goods and sales of assets as independent variables: the study employed regression analysis. The result revealed that the reported earnings of firms selling goods or assets to related purchases exhibit a low valuation coefficient than those of firms in China without such transactions, but this result is not observed during 2001–2003 after a new fair value measurement rule of related party transactions came into effect. Therefore the new related party transactions regulation in China is perceived to be effective at reducing the potential misuse of related party transactions for earnings management purposes.

Although most studies cover single measure of the earnings quality, Huang and Liu (2010) conducted a multivariate study of the relationship between related party transactions and firm value in high technology firms in Taiwan and China. Data were obtained from annual reports of listed high technology firms in Taiwan and China during the period 1998–2008. In a multivariate equation they investigated the effect of family shareholdings and related party transaction as the independent on return on equity (ROE), return on assets (ROA), market value added (MVA) and economic value added (EVA). The study employed multivariate ordinary least square method to test the hypothesis. The result revealed that the accounts receivable and account payable from related party transactions of high technology firms in Taiwan exhibit a significant positive relationship with performance. However, the sales or purchases of goods from related party transactions of high technology firms in China have a significant negative relationship with performance.

Some other studies did not find significant relationship between RPT and earnings quality. Pozzoli and Venuti (2014) investigated the relationship between related party transactions and financial performance companies and also to verify whether there is an association between these kinds of transactions and earnings management. Data from annual reports of listed Italian Companies for the period 2008–2011.

Using returns on assets as dependent variable while profit (or loss) from related party transactions as the independent variables, the study employed Pearson correlation. The result of the study revealed that the related party transactions and companies' financial performance are not correlated and that there is no evidence of a cause – effect relation. Therefore, related party transactions do not appear as a means used by Italian listed companies to realize earnings management, especially earning smoothing.

Likewise, Elhelaly (2014), conducted study on related party transactions, corporate governance & accounting quality in Greece among his investigation, he investigated the impact of related party transactions on accounting quality in Greece and association between related party transactions and earnings management. Data were obtained from annual reports of listed firms on the Athens stock exchange during the period 2009–2011. Using earnings management as dependent variable while related party transactions and corporate governance as the independent variables, the study employed multiple regression technique. The result revealed a negative significant relationship between earnings management and related party transactions. The finding does not support the conclusion that related party transactions are necessarily conducted to mask fraud or the extraction of firm resources. There is no significant difference in accounting quality between related party transactions firms and non-related party transactions firms.

Wang and Yuan (2012) conducted a study on the impact of related party sales by listed Chinese firms on earning informativeness and earnings forecasts. Secondary data were collected from the animal reports of listed firms on Shanghai stock exchange covering the period of 1998–2004 using return as the dependent variables while net income (market value) and related party sales of goods and services as the independent variables, the study employed regression analysis. The result revealed that earning of firms engaged in related party sales are at least 33% less informative after controlling for factors known to affect earnings informativeness. Financial analysts are overly credulous in their acceptance of earnings numbers that are contaminated by unreliable related party sales and provide less accurate and more optimistic earnings forecast for firms with more related party sales. Therefore, strong empirical evidence on the negative impact of related party transactions on the usefulness of accounting earnings data used by investors and financial analysts.

Based on the forgoing literature review it appears that works are largely from Far East Asia and rarely considered banks. We therefore formulate the first hypothesis for this study as below:

Ho1 *Related party transactions have no significant impact on earnings quality of listed deposit money banks in Nigeria.*

Earnings Quality and Off Balance Sheet Engagements

Generally, there is a dearth of studies that explore the relationship between OBSE and earnings quality although there are studies in closely related areas. However, Lozano–Vivas and Pasicuras (nd) investigated the impact of non-traditional activities on the estimation of bank efficiency. Data were obtained from unbalance data set of 4960 observation from 752 publicly quoted commercial banks operating in 87 countries between 1999 and 2006. Using cost efficiency and profit efficiency as dependent variable while off balance sheet items and non-interest income as independent variables, the study employed multi-product translog specification. The result revealed that inclusion off balance sheet items does not have a statistically significant impact on profit efficiency.

Also, Aktan, Chan, Zikovic and Evri-Mandaci (2003) conducted a study on off balance sheet activities impact on commercial banks performance from emerging market perspective. Data were obtained from the annual reports of listed banks on Istanbul stock exchange during the period 2001–2008 and analysed using multiple regression technique. The study investigated how banks risk profitability average and liquidity are influenced by off balance sheet activities of the banks. The result revealed that both bank specific risk and foreign exchange rate risk are positively related with off balance sheet activities. This indicated that off balance sheet activities increase bank-specific and foreign exchange risk exposure of banks in Turkey. The positive relationship might serve as a warning to banks speculative action using off balance sheet transaction in the market. Off balance sheet activities due to its hedging perception, improve banks stock returns but have a negative impact on return on equity. Off balance sheet activities do not have a statistically significant impact on leverage or liquidity.

Ge (2006) conducted a study on the implication of the off balance sheet treatment of operating leases for future earnings and stock returns. Data were obtained from COMPUSTAT annual data of firms for the period 1998–2004. Using future earnings and stock returns as proxy for earnings quality while operating lease activities as predictor variables, the study employed regression analysis. The result revealed that investors seem to incorrectly estimate the implications of off balance sheet lease activities for future earnings because operating lease activities has a negative relationship with future earnings.

Deyoung and Roland (2001) examined product mix and earnings volatility at commercial banks documenting evidence using degree of total leverage model. Data were collected from annual reports of 472 U.S. commercial banks over the 30 quarters March 1988–June 1995. The result revealed that replacing traditional lending activities with fee based activities – an ongoing trend that may be strengthened by recent financial modernization is associated with both higher revenue volatility and higher total leverage which in thus frame work implies higher earnings volatility

Lepetit, Nys, Rous and Tarazi (2006) conducted a study on product diversification in the European banking industry focusing on risk and loan pricing implications. An unbalanced panel data were obtained from the annual reports of European banks established in 14 European Countries for the period 1996-2002. The result revealed that banks expanding into non–interest income activities present higher risk than banks which mainly supply loans. Also higher income from other activities is associated with lower lending rates which suggest that banks may actually use loan as a loss. Lender altering default screening and monitoring activities and consequently risk pricing.

Irving & Smith (2014) examined off balance sheet arrangements and company performance during the recent financial crisis. Data were obtained from annual reports of companies in the CRSP monthly stock file cumulated across April 2006 – March, 2007 window. Using market –adjusted buy – and – hold returns and return on assets as dependent variable while off balance sheet arrangements as independent variables, the study employed regression analysis. The result revealed that off balance sheet arrangements are negatively and significantly associated with company performance measures during the financial crisis. They do not find the negative association for the pre-crisis period. And also found that companies using off balance sheet arrangements were exposed to more risk than companies not using off balance sheet arrangements. This is indicative that it is either despite their contingent nature OBSE are very risky or particularly risky items included in the observation they used.

Based on the forgoing literature review, again there appears to be hardly any Nigerian study focused on Nigerian banking sector which investigated the effect of OBSE on EQ of DMBs.

Also, the documented evidence is somewhat mixed leading us to formulate the second hypothesis for this study as follows:

Ho2: Off-balance sheet items have no significant impact on earnings quality of listed money deposit banks in Nigeria.

Theoretical Framework

This study is underpinned by Jensen and Meckling's (1976) agency theory which explains the problems that occur in agency relationships when either the interest of agent and principal conflict or when it becomes difficult or expensive for the principal to verify what the agent is actually doing (Elhelaly, 2014). The separation of ownership and control in modern business is considered the origin of the agency problem. An agency relationship is a contract under which one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent (Jensen & Meckling, 1976). If both parties in this relationship act opportunistically, there is a good reason to assume that the agent will not always act in the best interest of the principal (Elhelaly, 2014). Moreover, the principal also can limit deviations from his interest by forming proper motivations for the agent and by incurring monitoring costs designed to minimize the uncommon happenings of the agent (Jensen & Meckling, 1976).

It is also important to mention that in addition to the separation of ownership and control agency problem, there is type II agency problem. This problem occurs due to the conflict of interest between minority shareholders and controlling shareholders, where large owners in collusion with management use their power to dominate smaller ones (Berkman, Cole & Fu, 2009; Miller & Saradis, 2011). Thus, widespread use of RPTs and OBSE may be an indication for the presence of type II agency problem. Prior research have investigated and found evidence on the association between RPTs, and expropriation of firms' resources by controlling shareholders (Cheung et al, 2006; Cheung et al, 2009), OBSE and expropriation of firms' resources by controlling shareholders (Lozano–Vivas & Pasicuras (nd); Aktan et al., 2003).

This is because when concentrated ownership is dominating there is a conflict of interest between controlling shareholders and minority shareholders. Firms' managers in cahoots with controlling shareholders in some circumstance will manage their earnings in order to maximize benefits from outsiders like minority shareholders or even bond holders. Controlling shareholders are very likely to benefit from the use of RPTs and or OBSE as tools for earnings management to conceal their private control benefits from other shareholders (Elhelaly, 2014). Essentially, high level of RPTs and OBSE in the face of poor earnings quality among banks may be an indicator of an underlying agency problem where managers are securing advantages beyond the interest for the firm by booking substandard loans. RPT and OBSE as source of conflict of interest imply that it is most commonly used by controlling shareholders to expropriate the wealth of minority shareholders or conceal private control benefits. On the other hand, these RPTs like loans when securitized and sold off as investments are not kept on the bank's balance sheet but which are classified as off balance sheet items. So there is also the common likelihood of an intersection between the use of RPT and OBSE jointly to manage earnings indicating the presence of a wider agency problem.

Research Methodology

Data: Population and Sample

This study examines the impact of related party transactions and off balance sheet items on earnings quality of listed money deposit banks in Nigeria. The study covers a period of 4 years

(2011-2014). The CBN special audit was done between 2009/2010 while IFRS was adopted in 2011/2012. So the period of the study was chosen to coincide with the 2011.The study concentrated on those banks who posted their full annual reports throughout the sampled period (2011-2014). Out of the 15 DMBs listed on the Nigerian Stock Exchange, 10 banks constitute the sample of this study based on availability of data. The sample consists of Diamond Bank Plc., First Bank Plc., Guaranty Trust Bank Plc., United Bank for Africa Plc., Access Bank Plc., Zenith Bank Plc., Fidelity Bank Plc., First City Monument Bank Plc., Sterling Bank Plc., and Eco Bank Plc. The study makes use of documentary data obtained from the Annual Reports, Footnotes and Accounts of the 10 sampled banks representing 67 percent of the total population which met the required criteria for sampling.

Estimation Procedure and Model Specification

According to Beatty, Ke, and Petroni (2002), when earnings management or quality studies focuses on Loan Loss Provision (LLP), most studies use two-stage models - the first stage model is used to isolate the error term as discretionary component of reported earnings as against the non-discretionary model. Whereas the second stage model is used to evaluates the association between the discretionary accrual (earnings management) and the variables of interest. This study employed Ordinary Least Square (OLS) robust regression technique as a tool of analysis, where a two stage regression analysis was employed in order to first determine the residuals of Discretionary Loan Loss Provision (DLLP) the inverse of which is taken to represent earnings quality as a dependent variable and then subsequently used as input into the second stage regression model. The second regression model is used determine the relationship under investigation in this study.

Discretionary loan loss provision are not directly observed since in practice most of the bank managers determines the amount of loan loss provisions periodically according to individual risk assessment on potential uncollectable loans and loans write-offs (Abubakar, 2014). Consistent with Chang et al (2008) and Abubakar (2014), a

$$LLP_i / TA_{t-1} = \alpha_0\ 1/TA_{t-1} + \beta_1 LCO_i / TA_{t-1} + \beta_2 BB \text{ of } LLP_i / TA_{t-1} + e_i \quad (1)$$

$$^{1}DLLP_i / TA_{t-1} = LLP_t / TA_{t-1} - [\alpha_0\ 1/TA_{t-1} + \beta_1\ LCO_i / TA_{t-1} + \beta_2 BB \text{ of } LLP_t / TA_{t-1}] \quad (2)$$

cross sectional regression of loan loss provision is run against loans outstanding at the beginning of the period and charge-offs for the period. The difference between the error term and the total loan loss, beginning balance of loan losses on the other side, is used to determine discretionary loan loss provision for each period which represents the extent to which the DMBs have managed their earnings. To arrive at the extent of the quality of their earnings the difference between 1 and the calculated discretionary loan loss provision are taken for each observation. The result obtained is then inputted into the second stage regression model as dependent variable (earnings quality). It is mathematically shown as follows;

The lower the values of the DLLP/ TA_{t-1} which is represented by the residual, the higher the earnings quality (EQ) of the firms through loan loss provisions. The following regression equation used in this study to test the hypothesis is shown and explain in Table 1.

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[1] DLLP = Discretionary Loan Loss Provision (earning quality), LLP = Loan Loss Provision for firm i at time t; LCO = Loan Charge-offs for firm i at time t; BB of LLP = Beginning Balance of LLP for firm i at time t; TA t-1 = beginning Total Asset of firm i at time t; Ɛ = error term; α_0 = intercept; B_1 β_2 and β_2 = parameter estimates of the variables

$$EQ_{it} = \alpha_0 + \beta_1 RPT_{it} + \beta_2 OBI_{it} + \beta_3 SIZE_{it} + e_{it} \quad (3)$$

Table 1

Measurements of Variables

Variable	Type of variable	Definition and Measurement
EQ	Dependent	Earnings Quality measured as the residual of discretionary loan loss model
RPT	Independent	Measured as the absolute value of related party transactions scaled by total assets
OBI	Independent	Measured as the absolute value of off balance sheet items scaled by total assets
Size	Control	Measured as the log of total assets

Data Analysis and Discussion of Result

This section presents the results of the descriptive statistics, followed by the correlation matrix and regression results of the study.

Table 2 shows the minimum, maximum, standard deviation, skewness and kurtosis of the data use in the study. The table indicates the average earnings quality of Nigerian Listed Money Deposit banks as 1.48%, this figure ranges from -0.50% to 9.7% at minimum and maximum respectively. The volume of related party transaction is to the tune of 0.064% at an average, while this transaction ranges in volume from 0.000063% to 0.905501% at minimum and maximum respectively, indicating a sharp and sudden increase in the volume of this transactions. The table reveals that, off balance sheet items at an average stood at 0.324068%. This value ranges from 0.000379% to 1.00815%. The balance sheet items are also said to witness a fast increase during the period of the study. Furthermore, Size of these banks measured as natural log of their total asset, which is used as control variable, stood at an average of 14.52157%. The value of their total assets ranges from 0.00037% to 17.0037% minimum and maximum respectively, the value of skewness

Table 2

Summary of Descriptive Statistics

Variable	Observations	Mean	Std. Deviation	Min.	Max.	Skewness	Kurtosis
EQ	40	1.479511	2.173092	-0.50029	9.77414	2.384096	8.425634
RPT	40	0.063864	0.1507399	0.000063	0.90550	4.654857	25.81408
OBI	40	0.324068	0.243759	0.000379	1.00815	1.516509	4.522143
SIZE	40	14.52157	.9574669	0.00037	17.0037	1.177723	4.191638

ranges from 1.177723 to 4.654857 while that of Kurtosis ranges from 4.191638 to 25.8140.

Table 3 presents the correlation matrix which shows the relationship between the dependent and the independent variables and among the independent variables themselves.

Table 3 presents the correlation coefficients result which reveals that, there are no high correlations among the variables which could have been indicative of the possible presence of harmful collinearity among the variables of the study. The association between earnings quality and size which was found to be -0.4015

Table 3

Correlation Matrix

Variables	EQ	RPT	OBI	SIZE
EQ	1.0000			
RPT	0.1739	1.0000		
OBI	-0.1083	0.1200	1.0000	
SIZE	-0.4015	0.0103	0.3328	1.0000

as such is not high enough to be considered a strong negative correlation. So generally, none of the correlations between coefficients is above even 0.50 except for. The correlation of the coefficients may be considered to be harmful when it is approaching or above 0.80, Gujarati (2003). Table 3 reveals the correlation between earnings quality and related party transaction to be positive when earnings quality is at 1% level of significant. On the other hand, OBSE and size are negatively related with earnings quality. The result further reveals that OBSI and size are positively associated.

Presentation and Discussion of Result

Table 4 presents the regression result analyzed using OLS. The table shows the coefficient of various deterministic factors, their estimates, t-statistics as well as their probability value. This was followed by analysis of the relationship and significance or otherwise that exist between the dependent and the predictor proxies of the study. This was conducted by means of OLS robust as a result of the presence of heteroskedasticity in the data.

In the result obtained from the heteroskedasticity test conducted in this work, the chi-square value was 10.30 and the P value 0.0013 which is very significant, indicating heteroskedasticity was present. Therefore, as a result of the presence of heteroskedasticity, the Robust OLS which will automatically correct the problem of heteroskedasticity was used to estimate the relationship.

Table 4 show the summary of the estimated regression model which can mathematically be express as:

$$EQ_{it} = 14.23602 + 1.928202(PRT)_{it} -0.6114003(OBI)_{it}-0.8732883(SIZE)_{it} \quad (4)$$

Table 4

Presentation and Interpretation of Regression Result

Variables	Coefficient	Std. Dev.	t-statist	p-values	tolerance	VIF
Constant	14.23602	5.807786	2.45	0.019		
RPT	1.928202	0.806810	2.39	0.022	0.98	1.02
OBI	-0.61140	0.591528	-1.03	0.308	0.99	1.01
SIZE	-0.87329	0.376947	-2.32	0.026	0.99	1.01
R-Square	0.1852					
F-Stat	8.79					
Prob. (F. sig)	0.0002			0.0000		

The regression result shows that the model is fit because the F-Statistics statistics is 8.79 and is significant at one percent. The cumulative R^2 (0.1852) which is the multiple coefficient of determination gives the proportion of the total variation in the dependent variable explained by the independent variables together. Hence, it signifies that 19% of the total variation in EQ is caused by RPT, OBI AND SIZE.

From the result of the regression equation model above, the beta coefficient of RPT is approximately 1.93 (p-value of 0.022) which shows that there is a significant negative relationship between RPT and EQ of listed money deposit banks in Nigeria. The implication of the above result is that, for every one naira increase in the RPT, there is an approximate decrease of 1.93 Naira in the earnings quality of listed money deposit banks in Nigeria. This finding indicates that as the banks create additional number of related party transactions for instance by lending to their subsidiaries, the likelihood that the quality of their reported earnings will remain the same decreases. This could also imply that some of the related party lending by Nigerian banks are opportunistic as they tend to impair the quality of earnings. This finding supports the agency theory type II agency theory hypothesis which predicts the likelihood of expropriation of minority shareholders by management and block shareholders through RPTS. The finding is also in line with the empirical findings of studies by Munir, et al (2013), Elhelaly (2014), Cheung, et al (2006 & 2009), Aharony, et al (2010), Gordon and Henry (2005), Ge, et al (2010), Tsai, et al (2015), Huang and Liu (2010), and also Wang and Yuan (2012), but it is contrary to the findings of Kuan, et al (nd), Pozzoli and Venuti (2014).

OBSE is approximately -0.611 (p-value 0.308) which shows that there is a positive insignificant relationship between off-balance sheet item and EQ of listed money deposit banks in Nigeria. The implication of the above result is that, for every one Naira increase in off balance sheet item, there is an approximate increase of 0.611 naira in the EQ of listed money deposit banks in Nigeria. Given that for the relationship OBSE and EQ in this study we fail to reject the null hypothesis due to the high p-value, we therefore conclude that there is no sufficient evidence for us to argue that OBSE is likely to affect the EQ of Nigerian banks.

Conclusions and Recommendations

This study is conducted in other to examine the impact of related party transactions and off balance sheet items on earnings quality of the Nigeria money deposit banks. It was found out that related party transactions are negatively and significantly related to earnings quality. On the contrary, off balance sheet items were found to be negatively and insignificantly related to earnings quality. Based on the findings, the study concluded that related party transactions have significant impact on the earnings quality of the Nigeria money deposit bank. Management of the Nigeria money deposit banks should be inclined towards reducing the number of related party transactions with the view to improving the quality of their earnings. Regulatory authorities should encourage and focus on making sure that Nigeria deposit money banks comply with the standard guiding related party transactions. Standard setting bodies should consider increase the disclosure requirement for related party transactions.

Limitations of Study and Direction for Future Reearch

Although we consider the findings of the study relevant and one that is likely to lead to many future studies in the phenomena investigated the application of the findings of the study may be limited due to the limited number of observation used due to lack of availability of data. The scope of the study can be expanded in future studies to improve the robustness of findings in future studies.

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