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INTANGIBLE DISCLOSURE OF COMPANIES AND ITS ASSOCIATION WITH CORPORATE CHARACTERISTICS IN NIGERIA

Mahamad, T.

College of Business,
University of Utara, Malaysia

and

Salman, R.T (Mrs.)

Department of Accounting and Finance,
University of Ilorin,
Ilorin, Nigeria

Abstract

This paper examines the relationship between corporate characteristics and Intangible Assets Disclosure level in top hundred companies in Nigeria. The study used annual reports (secondary data) of companies listed in Nigerian stock Exchange as at July, 2010. The relationships were determined using intangible drivers under a number of hypotheses which were tested through regression analysis. The findings revealed that only 25% out of the sampled companies averagely disclose twenty to twenty five (20-25) percent of the total intangible assets. It was observed that intangible assets disclosures are significantly related with size of the company. The study concludes that with twenty-five percent of the sample companies revealing about 20 to 25% percent of the total intangible assets in their financial statement shows that reporting of intangible asset is very low in Nigerian Companies' context.

Introduction

Disclosure of financial information is mandatory in any organization in order to fulfil the regulatory obligation. Financial statement is a channel through which companies convey both tangible and intangible assets information (Holland, 2009). This financial information must be complete, accurate, adequate, relevant and timely for the users in order to make investment decision. Thus, both investors, creditors and financial analysts are dissatisfied with the content of financial statement which fails to report intangible asset information which is the most important aspect of investment decision (Christopher, 2010). If a company reports only tangible information leaving intangible aspects, such information is not complete and can cause information asymmetry (Holland, 2009). This study therefore, intends to examine the level of intangible asset information disclosure in the Nigerian coated Companies.

Intangible Assets (IA) are typically described as non-monetary economic goods without physical substance, but with a claim to future benefit (Lev, 2001). Both tangible and intangible assets are used in the production of goods and services. Intangible assets are divided into Structural Capital, Relation capital and Human Resource which has also been referred to by economists as Human capital. Human capital is the value of all the people within the organization and the benefits that can be obtained by utilizing their skills and knowledge. Structural capital is the structure and procedures within the organization that can be used by the employees to put their knowledge and skill to work, and documented processes that result from best-practices, such as Research and Development, IT capacity and software development. Relational capital is referred to as the capital that relates to the knowledge or market channels and the value of customer relationship of an organization. Intangible Assets in the financial statement is no longer a new issue in accounting field, as scholars like Flamholtz (1985), Brummet et. al. (1968) have made their contributions since 1960s.

However, the issue now is how accountants will report this important asset as its measurement and reporting has not been uniformly supported with standard. For example, Statement of Financial Accounting Standard (SFAS) Numbers 2 and 6 disagree with capitalizing Research and Development (R&D) expenditure but to expense it. In developed countries like US, UK Accounting Standards recognise R&D in line with International Financial Reporting System. But this is not the same in the developing countries like Nigeria. Nigerian Accounting Standard Board has just recently released Statement of Accounting Standard (SAS) 22 on how to report R&D in the financial statement in 2008. R&D is one of intangible driver that can be measured and valued in relation to firm value.

Apart from lack of uniformity in the accounting standard supporting the measurement in Nigeria, there is a problem of uniformity in the way and manner of presenting intangible assets in Nigerian companies, contrary to what operates in the developed countries. This is because in Nigeria, intangible assets (particularly structural and relational capital) reporting is very new as Nigerian Accounting Standard Board (NASB) just released SAS 22 (Accounting for Research & Development) which is one driver of intangible assets. Although before the release of SAS 22, companies in Nigeria were not mandated to disclose Intangible Assets information, they disclosed some intangible information voluntarily (Yahaya, 2007).

The main objective of accounting for intangible assets in the financial statement is to convey intangible asset information together with the tangible information to show case the overall value of a company (Lev, 2001). Guthrie (2001); Amir and Lev (1996); and Sveiby, 1997, believe that Human capital, Structural capital and Relational capital are assets that should be treated like tangible assets. They are of the opinion that without incorporating these assets in

the valuation of companies' assets, the "true" worth of such company would not be known. They hold this belief despite the fact that the monetary unit assumption of accounting does not allow for the reporting value of intangible asset in company's financial report. There are inconsistencies in the previous findings as regard the relationship between level of disclosure and industry type. Al- Mamum (2009) in Bangladeshi found a significant relationship between industry type and intangible asset disclosure level. Also, Ritter and Wells (2005) find that financial companies do disclose intangible asset information more than non-financial companies. Companies with a high level of Intangible Asset (IA) have relatively disclosed more of IA in their financial statement. But Matolesy and Wyatt (2007) in Australia, Wallace (1987) in Nigeria did not find any association between disclosure and industry type. The objective of this study therefore, is to examine the relationship between corporate characteristics and intangible assets disclosure level in top hundred companies in Nigeria.

Literature Review

Research on Intangible Assets can be traced back to the most fruitful research period in the late 1960's (Yahaya, 2007). Hermanson (1964) was the first person to attempt to include figure on human capital in the balance sheet, which became known as Human Resource Accounting. This was published in his pioneer work concerning the Valuation of Human Assets. Also in 1968, Brummet, Flanholtz and Pyle used the term "Human Resource Accounting" for the first time in their work and suggested the need to develop this area of accounting. Similar to these, is the work of Likert (1963). He was in support of human resource qualitative variables resulting in a better benefit in the future. During this period, numerous researches dealing with the influence of Human Resource Accounting information on decision-making were carried out. In the same vein, research works on structural capital especially R&D, Software development and IT capability can be traced back to the earlier works of Ben (1984); Amir and Lev (1996); Ballester, Livnat and Seethamraju (1996); Barth and Clinch (1998); Aboody and Lev (1998); Bharadwaj et. al., (1999). These works are all in support of reporting structural capital as asset that can be traced to company performance enhancement.

The same trend goes for relational capital, as many research works have been conducted to affirm the fact that relational capital should be treated like the physical asset in the financial statement. Some of the works include Borden (1942); Caves and Murphy (1976); Bublitz and Ettredge (1989); and Griliches (1990); which are based on economic effect of advertising, the importance of advertising and research and development in relation to intangible information, franchising; firms, markets and intangible asset respectively. The above works are testimonies to the earliest works on intangible asset.

Recently, scholars are still showing interest in the intangible asset information; such recent works include, Salamudin et al, (2010); Lu, Tsai and Yen, (2010); Holland (2009); Al-Twaijry (2009); and Al-Mamun (2009). Al-Twaijry work shows the relationship between intangible assets and future growth using Ordinary Least Square (OLS) method. His study revealed the corporate characteristic such as size, profitability and nature of company as having positively significant relationship to corporate growth. Likewise is the work of Salamudin et al (2010) in this regard.

To show a complete value of a company in this present day of information era, scholars have suggested the inclusion of Intangible Assets (IA) in the financial statement. Some of these scholars are Flamholt (1985); Brummet (1968) and Theeke & Mithell (2008). Yahaya, (2007); Al-Mamun (2009) and Okwy & Christopher (2010) are known for their work on Intangible asset (driver) specifically on Human Resource Accounting. These groups of scholars believe that reporting intangible asset drivers in the financial statement will provide complete information on the total value of a company upon which the financial statement users especially in investors would base their decision.

Intangible Asset drivers affecting the valuation of company could be analysed in a number of ways. First, it can be done by investigating the association between intangible asset drivers and company performance. Second, the strength of the relationship can be determined as either positive or negative. Prior researches show that there is a relationship between intangible asset drivers such as Human Resource, R&D, Software Development, IT capability, Patent and company performance and decision making. Notable among these works are Aboody and Lev, 1998; Flamholz (2005); Theeke and Mitchell, (2008); Kouhy, Vedd and Innes (2009); Al Mamun (2009); and Okwy and Christopher (2010). For example, the following studies examine the disclosure level and relevance of Intangible asset drivers to stock investment decision.

Okwy and Christopher (2010), examine human resource (intangible asset driver) and stock investment stock decision in Nigeria. They find that Human resource has value relevant to stock investment decision by investors. Their study further reveals that the quality of human resource is a major determinant in valuing firm stock in the capital market. Kouhy et al (2009) examines human resource policies, management accounting and organisation performance using sample from Canada, Japan and UK. Their finding reveals that the 'job for live' policy in relation to human resource is viewed as asset.

Also few scholars that examined structural capital driver such as R&D, Software Development Cost and IT capability are Aboody and Lev, 1998; Fukuni and Ushijima (2007); Al-Twaijry (2009) and Nasir (2006). Aboody and Lev (1998) examine 163 US software companies between 1987 and 1995. The study

reveals that companies that capitalized their software expenditure have value relevance and the value is positively associated with companies' share market.

Al-Twaijry examines R&D expenditure, corporate leverage and future growth using ordinary least square model (OLS). The result of the study shows that IA represent 1.2 % of the total assets and 1.3 % of total sales, while the regression result reveals that investment on IA forecasts 15% of the variation in a company's future growth. The summary of his work is that there is positive relationship between company future growths (dividend, leverage, sales) and R&D. Also the work of Nasir (2006) shows contribution of R&D, IT, Patent, trademark, company's secret to the overall performance of company. Again, Black et. al. (2006) and Fukui and Ushijima (2007) provide that R&D investment has statistically significant positive effects on future cash flow and firm value. Their results further reveal that as firm increase its investment on R&D, this creates larger market and in turn meeting consumers' and stakeholders' demand.

There are few theories in support of reporting of intangible asset driver in companies' financial statement. Such theories include resource and stakeholder theories. Resource Theory explains intangible asset in a more explicit way especially in relation to human resource (Al-Mamun, 2009). This theory believes in the competitiveness of a company. That is, competitiveness of a company depends on its uniqueness and not duplicated assets. And the most unique and not duplicated asset or resource of a company is its personnel. Even where many companies are on the same level of technology, the skill, ability and knowledge of the personnel of a company explain why that company will be more productive than others (Al- Mamun, 2009).

Stakeholder Theory also agrees with the reporting of Intangible Asset in the financial statement. This theory is of opinion that financial statement must be prepared to provide the necessary information useful for both stakeholders (Investors, management, financial analysts and creditors). The manager must therefore be ready to supply full information on both assets (tangible and intangible) to reduce information asymmetry (Holland, 2009; Abeysekera, 2007). There are many reasons why intangible assets must be included in financial reporting. The following are the reasons for including intangible assets in financial reporting. First, intangible assets are part of the overall assets of the company, which provide information about human capital, structural capital and relational capital and their values that can facilitate decision making by both investors and the management. Second, intangible information are the most useful information in the present information era (Salamudin et al, 2010). Finally, the intangible assets are the valuable assets used in the capital market to showcase the competitiveness of a company as long as they can be quantified (Rodgers, 2003).

On the presentation of Intangible Asset in the financial statement, Holland (2009) suggests that intangible asset should be reported in the notes to financial

statement since the existing Accounting Regulation do not permit the recognition and recording of some of intangible asset in the balance sheet. Presently, some of intangible drivers are reported in the profit and loss account as expense, especially, cost relating to human resource such as salaries, wages, and health allowance of staff Al- Mamun (2009). As intangible asset has been considered as crucial in valuation of company in capital market since its accounting and reporting are becoming important for company performances' measurement (Okwry and Christopher, 2010). Interestingly however, to date, no significant work has been done on intangible asset disclosure level especially in Nigeria context.

Methodology

a. The Model

This study uses multiple regression analysis model presented as;

$$Y_i = \alpha + \beta_1 \text{SIZE} + \beta_2 \text{FIN}_i + \beta_3 \text{PT}_i + e_i \quad (2)$$

Where

Y = Intangible Asset Accounting Disclosure Index (IADI)

α = inception of the regression line

β_i = coefficient (Slope of the regression line)

SIZE = Natural log of market capitalization is used as a proxy of size of the company

FIN_i (dummy variable) = Financial Institution, value 1 if the company is a financial institution and 0 if not

PT_i = Profitability is measured by operating income

e_i = Standard sample error.

The Intangible Asset Disclosure Index (IADI) is computed by using formula below, following Al-Mamun (2009)

$$\text{IADI} = \frac{\text{Total Score of individual Company} \times 100}{\text{Maximum Possible Score Obtained}}$$

Table 1: Measurement of Intangible Asset Accounting Reporting Items

No.	Disclosure items
1.	Research and Development
2.	Patent
3.	Goodwill
4.	Human Resource Development
5.	Employee categories
6.	Retirement benefit
7.	Number of employees
8.	Training & Development

9. Managerial remuneration
10. Health, safety & welfare of employees
11. Brands
12. Supply chains
13. Corporate Image
14. Franchising agreement
15. IT

In carrying out the analysis the study makes use of SPSS 14 version. The testing of the data normality was done with the help of Kolmogorov-Smirnov test which can be seen in table 5. Independent sample t-test was used to test Hypothesis 1. This is shown in table 7. Also, to show the impact of corporate characteristics on Intangible asset Disclosure of different companies in Nigeria, this study divides companies under study into financial and non-financial sectors.

b. Hypotheses of the Study

In order to have proper investigation into our set objective, the following hypotheses were set to be tested for;

Hypothesis 1: There is significant difference between financial and non-financial sector average IADI.

Studies relating to disclosure of Intangible asset reveal that there is a positive relationship between company size and level of disclosure (for example, Al-Twaijry, 2009; Al-Mamun, 2009; Yahaya, 2007. Al-Twaijry shows that there is a positive association between company size and company level of investment and disclosure of intangible. As in the case of Yahaya (2007), the present study does not focus on the issue of disclosure but rather on the cost allocated to human resource from the profit of the sampled companies. Hence, this study will like to test the hypothesis to investigate the association between size of a company and its IAD.

Hypothesis 2: There is a positive relationship between company size and level of Disclosure.

Guthrie (2001) avers that managers of a company with high profit will want to disclose both tangible and intangible information of their operation to show to the public where they have better competitive advantage. On the other hand, Vergauwen, Bollen and Oirson (2007) found that bigger firms provide more informative accounting disclosure than the smaller firms. Hence, this study sets

hypothesis to find the relationship between profitability and level of IA disclosure.

Hypothesis 3: There is a positive relationship between the profitability of a company and the level of IA disclosure.

c. Method of Analysis

This study made use of secondary data. The top hundred companies were selected based on price index report given by the Nigerian Stock Exchange (NSE) in their monthly report of July, 2009. All the companies used in this study were fully listed in the Nigerian Stock Exchange. These companies are categorised as financial and non-financial companies, such as Banks, Insurance, Oil and Gas, Manufacturing and others.

The secondary data source is preferred because this source presents these companies' true financial reports picture since they have been audited by external auditor as mandated by the Nigerian Accounting Standard Board (NASB) and approved by Securities and Exchange Commission (SEC) as well as NSE. Hence, the information derived from the financial statements are considered to be reliable and acceptable (Abeyesekera, 2007).

Intangible Asset Accounting Reporting (IAAD) variables (table 1) were arrived at from relevant literature, past work and the disclosure items of the selected companies from their annual reports. In assessing each of these Intangible Asset Disclosure items, a dichotomous procedure was used where individual company was assigned with a score of "1" if the company appears to have disclosed an item of reporting variable and "0" if not. And at the end of the exercise, the score of each company was totalled to find the net score of the company.

Results and Discussions

Level of intangible asset disclosure

Table 2 presents the distribution of the Intangible Asset reporting levels in term of number each items disclosed as percentage of the total disclosure variables. The modal class of IAD items is 20-25 percent indicating that maximum twenty-five companies IA disclosure level is 20 to 25 percent while nineteen (19) companies disclose 15 to 20 percent of the disclosure items. The table also reveals that the IAD of 85 percent of the sample companies are less than 40 percent disclosure items. The remaining 15 percent companies have IAD between .25 and .45. This shows that the level of Intangible Asset Disclosure of listed companies in Nigeria is very low.

Table 2: Intangible Asset Reporting Levels

Range	No. of Company	Company in %	Cumulative %
10 – 15	15	15	15
15 – 20	19	19	34
20 – 25	25	25	59
25 – 30	16	16	75
30 – 35	10	10	85
35 – 40	6	6	91
40 – 45	0	0	91
45 – 50	6	6	97
50 – 55	3	3	100
55 – 60	0	0	-
Total	100	100	-

Table 3: Descriptive Statistics of the IAD Indexes

	N	Minimum	Maximum	Mean	Std.Deviation
IADI	100	6.52	50.35	39.52	11.33
Valid N	100				

Medium of Intangible Asset Reporting

Table 4: shows that 59.40% of the total disclosed Intangible Asset information is reported in the notes to financial statement and less 3.12% is reported through chairman's report which is informal. 18% is reported formally through profit & loss account and balance sheet.

Table 4: Medium of IAA Reporting

Medium of Reporting	No. of Information Reported	Percentage (%)
Balance sheet	3	4.68
Profit & Loss Account	15	23.43
Notes to the Accounts	38	59.40
Statement of value Added	3	4.68
Directors' Report	3	4.68
Chairman's Report	2	3.12
Total	64	100

Hypotheses Testing

The Kolmogorov-Smirnov Test (see table 5 in appendix) reports the significant value .001 which shows that the sample data were normally distributed. Pallant (2001) avers that if the sig. value of more than .05 a non-

significant result. Table 6 a (see in appendix A) presents descriptive statistics and table 6b shows correlation results of relevant variables. The result reveals that type of company (financial company) is negatively correlated with IADI while natural log of market capitalization which represents size is positively correlated with IADI likewise the profitability.

Table 7 (see appendix) reveals the significant value for the independent sample t-test .005 which is less than .05. It thus support the hypothesis 1 that says there is significant difference between financial and non-financial company average of IADI. It goes further to show that the alternative hypothesis of equal variance not assumed is accepted as significant value of Levene's Test .000 is more than a value of .05. Therefore, the assumption of equal variance for the null hypothesis of equality of means cannot be accepted, because the average IADI of financial and non-financial companies are significantly different.

For the association of IAAD with corporate characteristics, a multiple regression model was run. The multiple correlation coefficient (R) is 0.879 ($R^2 = 0.657$) and the adjusted $R^2 = 0.625$, indicates that 63% of the variation in Intangible Asset Disclosure index can be predicted from the independent variables (see table 8a in appendix). The coefficient results show that the size of the company (natural log of the market capitalization) has a positive relationship with IADI with Beta=.268, sig. Greater than .05. (See table 8b in appendix). Even when compare the coefficient of MC (size) that is half of Beta with standard error this variable is still significant (0.566 is greater than 0.564). This shows that the bigger companies disclose larger extent of Intangible Asset Accounting Information. Then, the hypothesis 2 is accepted, that there is a significant and positive relationship between company size and level of Intangible Asset Accounting Disclosure.

The regression also shows that there is a positive relationship between profitability and IADI with Beta =-.208, sig.05 although the relationship is weak but not significant because its coefficient is less than the standard error. This indicates that managers of companies with high profit at the end of the year may not disclose IAA information. Therefore, hypothesis 3 is rejected.

Conclusion

Intangible Asset Accounting information of an organization is as important as tangible asset information in investment decision making in this era of information-based economy. The importance of Intangible Asset reporting in any organization cannot be over emphasised in this present information era. In the light of this, most companies do disclose their Intangible asset information voluntarily especially in Nigeria since there is no sanction for any company that refuse to disclose their intangible asset information. In fact, those companies that do disclose their intangible asset information do it to showcase where they have

competitive advantage over others, and these are shown, in most cases, in the note to accounts and value added statement.

This study had examined the relationship between corporate characteristics and Intangible Asset Accounting Disclosure of public listed companies in Nigeria. The findings from the study show that the size of the company is significantly associated with IADI. And it is further revealed that the bigger companies do disclose more in term of intangible asset information than the smaller companies. This result is in line with Abeysekera, (2009) findings which reveal that the bigger companies do disclose their intangible asset information because of their maturity in the capital market and also to uphold market value.

Similarly, the result reveals that financial companies disclose more of Intangible Asset information than non-financial companies and also profitability does not have any effect on the level of disclosure of intangible asset information in the financial reporting.

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