

Effect of Inflation Accounting on Business Income Measurement of Quoted Manufacturing Companies in Nigeria.

Akabom Ita Asuquo, Ph.D., FCCA , Fadenipo Adesola Adenike, ACA, B.Sc. (HONS) , Ogbeche Linus Ogar, B.Sc. (HONS), Ahonkhai Ohimai Ebahi B.Sc. (HONS) & Grace Edet Okon B.Sc. (HONS)
Department of Accounting, Faculty of Management Science
University of Calabar, P.M.B 1115 Calabar, Nigeria

Abstract: *The study evaluates the effect of inflation accounting on business income measurement of quoted manufacturing companies in Nigeria. It specifically examined the historical cost and the current cost accounting measure in relation to companies profit level with regards to depreciation cost, tax and dividend. To this end, historical cost and current cost extracts of six manufacturing companies for the period of [2011-2015] were used for the study. Multiple regression (ordinary least square method) was used for the analysis of the data and it was discovered that accounting methods have a significant effect on business income, and that the profit under the historical cost accounting was higher than that of the current cost costing. It was recommended that companies profitability level should always be evaluated based on the purchasing power of money in order to know the actual worth of the company.*

Keywords: *Inflation accounting, business income, reported profit, historical cost, current cost, capital maintenance, purchasing power, financial statements*

1. Introduction

Financial statements are reports of enterprise financial transactions. These transactions are to be presented fairly and accurately using the relevant policies and regulations which are enforced by the regulatory authorities in such economy. Users of financial statements depend on the information of such statements for decision making, the manner in which the content of financial statements are measured and presented is therefore of utmost importance [Igben, 2004]. Traditionally, historical cost is the basis used in the periodic preparation of financial statement, which is an approved policy for most countries. There have been heavy criticisms of

the historical cost theory for its obvious deficiency of ignoring the effect of price changes on transactions and assets resulting in overstatement of profit consequently paying higher tax and dividends. The relevance of financial statements can be greatly enhanced if such statements can be prepared using methods that can present the information fairly and more reliably. Several scholars have posited other income measurement theories such as the current cost theory, net realisable value theory, current purchasing power theory and others in a bid to bring closer to market relevance the values of transactions and assets as presented by the financial statements [Ola, 2001].

An economic entity will prefer an income that is measured in real terms taking into account the effects of inflation in order to establish the true purchasing power of such income or profit. When financial statements are measured and presented on historical cost basis, such statements ignores the effects of changes in price levels of assets and transactions. This study seeks to show the relationship between the major determinants of reported profit prepared in Historical Cost theory and Current Cost theory. The analyses shall show whether the major components of profit chosen for this study which are total revenue and depreciation, tax and dividend have any significant influence on the reported profit using the two theories mentioned above.

Performance measurements through financial reporting affect all stakeholders of an organisation; therefore any modification on the measurement basis could have broad effects. Controversies now encircle the basis of measurement of income or profit via historical cost accounting. It is argued that the concept conflicts with the going concern concept of measurement especially when there is a change in value of money. It is however believed that income

measurement should be based on current costs to so as to depict the effect of changes in monetary value of transactions and items reported in the financial statements [ICAN study pack, 2014].

The objective of this study is to examine the difference between the effect of depreciation, tax and dividend on reported profit computed using current cost accounting theory and historical cost accounting theory.

2.1. The Concept of Capital Maintenance

The capital maintenance concept gained prominence with the definition of income (profit) of Hicks [1946] as 'the maximum value that an individual can consume at any given time and still expects to be well off at the end as he was at the beginning'. The concept of capital maintenance posits that a company should be at a better capital position at close of the period than it was at the start of the period.

Different approaches exist in the determination of the income, and this has an effect on the capital of the firm. Some approaches keep capital constant as at the beginning and at the end of business. This approach computes dividends as a function of the surplus profit that keeps the value of capital constant both at the beginning and at the end of the period. Some consider distribution of dividends as a depletion of capital; this approach retains all or some percentage of profits in the business for capital growth;

Financial Capital Maintenance measures in real terms the increase of shareholders stake in the firm by adjusting their interest for the effects of inflation. In a period where there is no capital injection or withdrawal, real profit can be determined as the difference between capital stated in real terms at the beginning of the period and capital stated at the completion of the period in real terms.

The Conceptual Framework in existence explains following capital maintenance concepts:

2.1.1. Financial Capital Maintenance.

This considers only profits that are earned in monetary terms; the net worth of assets at the expiration of a particular period in excess of the net worth of assets at the commencement period (in monetary terms), after adding contributions from and reducing distributions to owners during the period. Financial capital maintenance is measured using either nominal monetary units or units of constant purchasing power. Richard, L. & David P. [1996]

Essentially, the end users of financial information are more concerned about how the financial capital of an entity is maintained.

Assets – Liabilities = Equity

Opening equity (net assets) + Profit – Distributions = Closing equity (net assets)

There are also two ways of looking at financial capital maintenance, PWC [IFRS 2010]:
money financial capital maintenance,
real financial capital maintenance

In **money financial capital maintenance**, profit is achieved where closing net assets surpass the opening period net assets, and each net asset is measured at historical cost basis.

The method doesn't take into consideration any inflation or the time value of money.

In **real financial capital maintenance**, an entity makes profit only when the closing net asset is greater than the opening net assets, and both of these figures are measured at current prices. The method takes into consideration the effect of inflation and time value of money.

2.1.2. Physical Capital Maintenance.

Profit under this concept, is considered earned when an entity's physical productive capacity or operating capacity necessary to attain a set capacity level at the expiration of the period surpasses the physical productive capacity at commencement of the period, after deducting distributions and contributions to and from the business owners during the period.

Most entities adopt financial concept of capital maintenance. The management of the organisation can however exercise their discretion to choose the capital maintenance concept that presents the more useful financial information to the users of financial statements. [Casmir, 2014].

2.2. Concept of Income And Profit

Income refers to economic benefits earned by an organization from its operations and other activities. Income is defined in accounting as the profit earned for a period usually one year, this profit is obtained as the positive difference between the total revenue received for a period and the expenses incurred to generate such revenue.

Accounting profit is simply measured as the difference between the total revenue earned in a period and the expenses and costs of assets employed to earn such revenue. However, in the

determination of the profit earned, measurement of depreciation and other associated assets costs, accountants adopt the use of historical cost accounting. Economic profit on the other hand is measured in terms of surplus assets at close of a period over the worth of assets as at the time the business commenced.

Gay [1993] defined "Income as the change in purchasing power possessed by the entity between two points in time. This definition supports the economic view of the concept of income which defines income as a positive change in a company's capital between the beginning of the year and the end of the year". Income measurement is very crucial to every organization. The value of capital is dependent on the measurement of income of the organization. Capital growth is a function of the income generated during the year and new capital introduced during the period. The Sandilands Report states that "a company's profit is the maximum value that a company can distribute during the year and still expect to be as well off at the end as it was at the beginning of the year". Robson, K. [1994]. The report stated the above theory in an equation as

$$P = D (A_2 - A_1)$$

Where P is Profit for the period
D is dividends distributable
A₂ is Assets at year end
A₁ is Assets at beginning of year.

Where P = D then A₂ = A₁, this signifies that the company distributes all the profit earned as dividends therefore the capital position at the close of the period is the same as the start of the period.

Where P > D then A₂ > A₁, this signifies that the company distributes just a part of its profit as dividends, therefore a capital growth will be experience, hence the position of the company's year-end capital is healthier than the capital at the beginning of the year.

Where P < D then A₂ < A₁, this signifies that the company's profit is less than the amount distributed as dividends, therefore a capital degradation is experienced, hence the capital position for the beginning +of the period is better than the position at the close of the period.

2.3. Theories of Income Measurement

Several theories of income measurement have been propounded over time. These theories differ in terms of the accepted variables used in recognizing and value assets. The cost of operation of any organization is depended on the assets and expenses associated with using the assets to generate revenue,

Paul [2010]. Historical Cost Theory which is regarded as the traditional method of accounting basis has been the overtime the main basis for recording transactions.

2.3.1. Historical Cost Based Income Measurement

This is the traditional approach to measuring income of businesses. The historical cost theory accounts for items in the financial statement in their original cost ignoring inflation effects. This method is specified by the International Financial Reporting Standards [IFRS] for preparing financial statements of companies and businesses. The historical cost theory is simple to apply and it shows the original cost of assets used by the organization. "Using this method, profit is determined by comparing sales revenue with the historical cost of the asset sold. It has been discovered that where prices are rising rapidly, the historical cost theory may significantly understate the value of the economic resources employed in the business", Meigs [1984].

Simon, J. R. [1987] provides that the historical cost theory leads to an estimation of profit that leads to high tax deduction, dividends payments and capital depletion.

Barry [1980] posits that "reliance on Historical Cost Theory in the face of inflation has been criticized. Among these are:

The substantial under valuation of current value of the net book value of fixed assets

The balance sheet figure for stock reflects price ruling at the date of purchase or manufacture rather than those at the year end.

Changes made in arriving at the profit do not reflect the current value of assets consumed, the effect being to exaggerate the profit in real terms.

No account is taken of the effect of increasing price on monetary items

The understatement of asset prevents a meaningful calculation of returns on capital employed".

Rapid price changes in the last 2 decades have significantly influenced experts' perception of the financial statements of entities prepared on Historical Cost Basis. This theory provides basis for objectivity, simplicity, comparability, verifiability and measurability, Millichamp [1989] and Hendriksen [1982]. However in periods of inflation, values used in financial statements have no relevance on current values of items. In recent times, there have been several calls for financial statements to contain relevant values of assets, liabilities, incomes and expenditures affect taking into account the effect of inflation. In other to repel the deficiency of historical cost accounting measurement basis, some adjustments have to be made to reflect price level changes. These are

referred to as inflation accounting methods. Four main methods considered for adjusting for inflation include:

Current Cost Accounting Theory
Current Purchasing Power Accounting Theory
Replacement Cost Accounting Theory
Net Realizable Value (Exit value) Theory

2.3.2. Current Cost Accounting Theory

"Current Cost Accounting is concerned with the value of net asset to the business and combines replacement cost, realizable value and present value that should be attached to such assets", Meigs [1984].

The current cost theory lies heavily on the going concern concept; assets are valued on their present values taking into account price level changes and other factors that affect the values of assets.

It is largely believed that the current cost theory supports capital maintenance of the entity. Profits obtained through this theory reflects the actual surplus a business earns after comparing its revenue with the cost of assets taking into account price changes due to inflation.

Under current cost, the value of all inputs and assets used in the course of deriving income within an accounting period are recognized based on their "current value at the time of consumption or realization" [Anao, 1987].

Current cost theory attempts to reflect the cost of operations and assets in the true present day value consequently, profit obtained using this theory will better portray the performance of the organization.

Current cost theory provides the advantage of matching current cost of operations with current revenue generating these revenues. The current cost theory also provides a more meaningful basis for predictive decision making since the financial statement reflects the trend of price changes which is prevailing in the economy. Jones [2009]

Current cost theory has been majorly criticized on the bases of not taking into consideration the fact that the gain resulting from historical cost conversion to current cost is merely a paper figure which is not supported by a physical asset in the organization.

2.3.3. Current Purchasing Power Accounting Theory

Current purchasing power accounting(CPPA) theory posit that the actual price of an asset is fair and accurate if the historical cost of the asset is adjusted to current cost; by taking into consideration the price changes level using the General Price Index (GPI).. The method use the official, approved

and established general price index (GPI) as a basis of conversion to reflect changes in general price level historical cost based income statements and statements of financial position. The method supports the presentation of financial statements with regards to equal purchasing power unit. [Glautier & Underdown, 1986; Anao, 1987; Blake, 1959]

Characteristics of Current Purchasing Power Theory

An additional financial statement is required to be prepared and incorporated into the financial statement prepared on historical cost basis. The additional statement includes the restated income statement as well as the restated financial position statement.

Historical cost based financial statement is the appropriate basis used in preparing a statement under the current purchasing power.

The indexes or indices used for restating items recorded in historical cost are consumer price, wholesale price indices or general price index.

Items of financial statements prepared using current purchasing power are basically categorized into monetary and non-monetary items. Whereas adjustment is required for non-monetary items, no adjustment is needed for monetary items.

Monetary items net losses or gains are usually included in the income statement.

Non-monetary and Monetary Items

Non-monetary Items

This refers to items that lack the ability to be given a specific or known amount of cash. They are assets whose value relies on economic situation; they do not have fixed exchange of cash value. They include: equipment, plant and machinery, land and building and inventory.

Monetary items

These include assets such as bank deposits, cash, and accounts and notes receivable. They can readily be converted into a determinable or fixed amount of currency.

2.3.4. Replacement Cost Theory

A business which is going concern is expected to constantly replace its assets within the normal business operations. Hence, the entity's assets are restated using current replacement costs and therefore matched with the current revenues earned by such assets [Glautier and Underdown, 1986].

Measurement of business assets on replacement cost does not necessarily give the same value as measurement on current cost basis. While current cost takes into account the inflation effect on price, replacement cost will go a step further to consider peculiar situations affecting individual such as scarcity, government embargos etc.

A business profit is the surplus of current revenue less cost of operations including depreciation measured on current cost of replacement

This theory ensures that assets are measured in values that reflect current prices changes and specific phenomena that affect individual assets which could result in variation in prices of such assets.

Replacement cost theory provides business advantage such that the value shown in the account is the actual price for which such assets will be placed where the need arises. This provides business forecast and efficient planning opportunities.

Replacement cost theory enables businesses to properly maintain their capital. Profits are stated in current terms thus reflecting the current price factors and assets variables. Profits distributed as dividends will reflect the actual surplus earned by the business during the financial year and not a false surplus, based on historical cost.

2.3.5. Exit Value (Net Realisable) Theory

This theory provides for assets to be measured in their disposal values. The business assumes a status of liquidation thus stating all assets in their current market values for non-related (arm’s length) party disposal transactions [Anao, 1987].

The theory also posits that liabilities should be carried at their current settlement values. However, liabilities and assets are estimated based on the value of cash that will be paid or received when these items are realized.

The values used in this theory are undiscounted and not adjusted for any factor including inflation. This value is mostly used by a valuator during liquidation. Muller, G. [1997]

3.0. Research Methodology

Design for the study is expo facto and exploratory research designs. The population for this study include the quoted companies on the Nigerian Stock Exchange (NSE). The population was selected based on the fact that they are under obligation to follow the stipulated rules, principles, and standards required of them in the preparation and publishing

of their financial statements by Securities and Exchange Commission (SEC) and Financial Reporting Council (FRC). Moreover, financial statements depict the economic information and financial activities of organizations, thus providing necessary data for testing the hypothesis of this study. Data from six quoted companies were used for the study and data collected were majorly secondary data.

3.1. Model Specification

The study adopted the multiple regression (ordinary least square) technique, with an identifiable model stipulated as:

Model 1: $RPHCA = f(DEP, TAX, DIV)$

Model 2: $RPCCA = f(DEP, TAX, DIV)$

The above models are statistically stated as thus:

$RPhc = b_0 + b_1DEP + b_2TAX + b_3DIV + e_i$ -----1

$RPcca = b_0 + b_1DEP + b_2TAX + b_3DIV + e_i$ -----2

- P_{hc} =Historical Cost Accounting(Profit)
- R_{Pcca} = Current Cost Accounting (Profit)
- DEP = Depreciation
- Tax = Taxes
- DIV = Dividend
- b₀ = Intercept
- b₁ – b₃ = Parameter

4.1 Data Analysis and Presentation

Table 1 :Historical Cost extract

| Year | 2011 | 2012 | 2013 | 2014 | 2015 |
|--------------------|----------------|----------------|----------------|-----------------|-----------------|
| | '000 | '000 | '000 | '000 | '000 |
| Company I | | | | | |
| Reported Profit | 6,636,335.00 | 7,913,503.00 | 4,859,019.00 | 7,440,102.00 | 10,691,060.00 |
| Depreciation | (1,601,225.00) | (2,482,254.00) | (2,917,956.00) | (2,953,196.00) | (3,012,484.00) |
| Taxation | (3,265,333.00) | (7,773,991.00) | (1,417,148.00) | (3,999,666.00) | (4,193,390.00) |
| Dividend | (2,654,866.00) | (5,604,717.00) | (6,194,687.00) | (3,539,821.00) | (4,719,762.00) |
| Company II | | | | | |
| Reported Profit | 5,086,403.00 | 8,254,557.00 | 10,900,524.00 | 18,942,856.00 | 25,700,593.00 |
| Depreciation | (5,444,802.00) | (5,242,888.00) | (4,967,791.00) | (5,019,464.00) | (63,557,667.00) |
| Taxation | (4,061,735.00) | (4,643,189.00) | (5,535,731.00) | (8,933,480.00) | (11,818,521.00) |
| Dividend | (4,159,409.00) | (4,915,666.00) | (9,075,075.00) | (12,024,474.00) | (36,687,428.00) |
| Company III | | | | | |

| | | | | | |
|-------------------|----------------|----------------|----------------|----------------|----------------|
| Reported Profit | 3,380,667.00 | 4,429,884.00 | 3,377,481.00 | 1,603,456.00 | 2,070,045.00 |
| Depreciation | (249,917.00) | (407,701.00) | (801,871.00) | (1,270,217.00) | (1,658,718.00) |
| Taxation | (1,512,220.00) | (2,089,365.00) | (1,573,983.00) | (911,167.00) | (1,360,896.00) |
| Dividend | (2,500,000.00) | (3,393,000.00) | (2,193,750.00) | - | - |
| Company IV | | | | | |
| Reported Profit | 161,455.00 | 201,571.00 | 312,748.00 | 351,528.00 | 735,642.00 |
| Depreciation | (17,774.00) | (16,116.00) | (17,234.00) | (14,476.00) | (23,697.00) |
| Taxation | (261,634.00) | (215,160.00) | (143,652.00) | (101,098.00) | (89,387.00) |
| Dividend | (115,500.00) | (147,000.00) | (105,000.00) | (157,500.00) | (420,000.00) |
| Company V | | | | | |
| Reported Profit | 59,175.00 | 98,427.00 | 82,228.00 | 116,415.00 | 98,265.00 |
| Depreciation | (5,480.00) | (5,857.00) | (4,887.00) | (9,526.00) | (18,369.00) |
| Taxation | (29,980.00) | (55,175.00) | (42,364.00) | (55,891.00) | (68,863.00) |
| Dividend | (24,631.00) | (37,010.00) | - | (65,414.00) | (79,799.00) |
| Company VI | | | | | |
| Reported Profit | 1,759,468.00 | 2,422,530.00 | 1,716,208.00 | 1,131,103.00 | 1,718,579.00 |
| Depreciation | (576,021.00) | (591,317.00) | (713,496.00) | (8,697,680.00) | (1,009,159.00) |
| Taxation | (225,993.00) | (971,373.00) | (819,237.00) | (633,542.00) | (825,032.00) |
| Dividend | (1,563,000.00) | - | (2,187,611.00) | (1,716,433.00) | (1,129,865.00) |

Source: audited financial statements of the relevant quoted companies [2011-2015]

TABLE 2

Regression result on the effect of business income (reported profit) on depreciation, tax and dividend using both historical cost accounting

| INDEPENDENT VARIABLE ERROR | ESTIMATED COEFFICENTS | T-Statistic | P- Value |
|----------------------------|-----------------------|-------------|----------|
| Constant | 1312.053 | 3.5090 | 0.0000 |
| DEP | -0.0020 | -2.0225 | 0.0010 |
| TAX | -2.4902 | 2.7801 | 0.0020 |
| DIV | -0.2464 | 3.3742 | 0.0000 |
| R | | = 0 | |
| .9758 | | | |
| R-Square | | = 0 | |
| .9522 | | | |
| Adjusted R-Square | | = 0 .8438 | |

SEE = 135932.5832
 F - Statistic (df1=3 & df2=6) = 14.0145
 Durbin Watson Statistic = 2.8443

DEPENDENT VARIABLE: Reported Profit (RPHC)

Source: SPSS, output, 2015

Table 3 : Current Cost extract

| Year | 2011 | 2012 | 2013 | 2014 | 2015 |
|--------------------|----------------|----------------|----------------|-----------------|-----------------|
| | '000 | '000 | '000 | '000 | '000 |
| Company I | | | | | |
| Profit | 5,972,701.50 | 7,122,152.70 | 4,373,117.10 | 6,696,091.80 | 9,621,954.00 |
| Depreciation | (1,761,347.50) | (2,730,479.40) | (3,209,751.60) | (3,248,515.60) | (3,313,732.40) |
| Taxation | (3,591,866.30) | (8,551,390.10) | (1,558,862.80) | (4,399,632.60) | (4,612,729.00) |
| Dividend | (2,920,352.60) | (6,165,188.70) | (6,814,155.70) | (3,893,803.10) | (5,191,738.20) |
| Company II | | | | | |
| Profit | 4,577,762.70 | 7,429,101.30 | 9,810,471.60 | 17,048,570.40 | 23,130,533.70 |
| Depreciation | (5,989,282.20) | (5,767,176.80) | (5,464,570.10) | (5,521,410.40) | (6,913,433.70) |
| Taxation | (4,467,908.50) | (5,107,507.90) | (6,089,304.10) | (9,826,828.00) | (13,000,373.10) |
| Dividend | (4,575,349.90) | (5,407,232.60) | (9,982,582.50) | (13,226,921.40) | (40,356,170.80) |
| Company III | | | | | |
| Profit | 3,042,600.30 | 3,986,895.60 | 3,039,732.90 | 1,443,110.40 | 1,863,040.50 |
| Depreciation | (274,908.70) | (448,471.10) | (882,058.10) | (1,397,238.70) | (1,824,589.80) |
| Taxation | (1,663,442.00) | (2,298,301.50) | (1,731,381.30) | (1,002,283.70) | (1,496,985.60) |
| Dividend | (2,750,000.00) | (3,732,300.00) | (2,413,125.00) | - | - |
| Company IV | | | | | |
| Profit | 145,309.50 | 181,413.90 | 281,473.20 | 316,375.20 | 662,077.80 |
| Depreciation | (19,551.40) | (17,727.60) | (18,957.40) | (15,923.60) | (26,066.70) |
| Taxation | (287,797.40) | (236,676.00) | (158,017.20) | (111,207.80) | (98,325.70) |
| Dividend | (127,050.00) | (161,700.00) | (115,500.00) | (173,250.00) | (462,000.00) |
| Company V | | | | | |
| Reported Profit | 53,257.50 | 88,584.30 | 74,005.20 | 104,773.50 | 88,438.50 |
| Depreciation | (6,028.00) | (6,442.70) | (5,375.70) | (10,478.60) | (20,205.90) |
| Taxation | (32,978.00) | (60,692.50) | (46,600.40) | (61,480.10) | (75,749.30) |
| Dividend | (27,094.10) | (40,711.00) | - | (71,955.40) | (87,778.90) |
| Company VI | | | | | |

| | | | | | |
|-----------------|----------------|----------------|----------------|----------------|----------------|
| Reported Profit | 1,583,521.20 | 2,180,277.00 | 1,544,587.20 | 1,017,992.70 | 1,546,721.10 |
| Depreciation | (633,623.10) | (650,448.70) | (784,845.60) | (9,567,448.00) | (1,110,074.90) |
| Taxation | (248,592.30) | (1,068,510.30) | (901,160.70) | (696,896.20) | (907,535.20) |
| Dividend | (1,719,300.00) | - | (2,406,372.10) | (1,888,076.30) | (1,242,851.50) |

Source: audited financial statements of the relevant quoted companies [2011-2015]

Table 4
Regression result on the effect of business income (reported profit) on depreciation, tax and dividend using current cost accounting

| INDEPENDENT ESTIMATED VARIABLES COEFFICIENTS | STANDARD T-Statistic | | P- Value | |
|--|----------------------|----------|----------|--------|
| | ERROR | | | |
| Constant | 798.1423 | 235.3466 | 3.8725 | 0.0000 |
| DEP | -0.3845 | 0.1390 | -2.7423 | 0.0018 |
| TAX | -0.1790 | 0.0581 | 2.8967 | 0.0010 |
| DIV | -0.9482 | 0.2781 | 3.3922 | 0.0000 |

R = 0.9550
 R-Square = 0.9120
 Adjusted R-Square = 0.8830
 SEE = 56928.01564
 F-Statistic = 24.9272
 Durbin Watson Statistic = 1.1247

DEPENDENT VARIABLE: Reported Profit (RPCCA)

SPSS, output, 2015

4.2. Results of Data Analysis

Table 2 above is the regression result derived from the information in table 1. It reveals the effect between business income/reported profit (dependent variable) and depreciation, tax and dividend (independent variables) using historical cost accounting. The result of the regression analysis indicates that the coefficient estimates of the regression parameters conformed to our economic expectation as shown in the negative signs of the parameters. This implies that the independent variables which include depreciation, dividend and taxes; negatively influence reported profit which is the dependent variable. This indicates that a reduction on the dependent variable that is; reported profit is caused by an increase in the independent variables.

The R-square; 0.9522 indicates that 95.2% of the sampling variation of the dependent variable is explicable caused by the variables which can be explained while 4.7% cannot be explained. The

remaining 4.7% could be resulted from other variables not structured in the model. The R-square value indicates a significant relationship between the dependent and explanatory variables.

The adjusted R-square value is 0.8438. This indicates that the explanatory variable is responsible for about 84% variation in profits, while about 15% of the variation is accounted for by the error term.

To test the statistical model significance, F-statistics was applied. The outcome is at 5% significant level, this is due to the fact that F-statistics calculated value of 14.0145 is higher than 4.76 which is the table value at df1=3 and df2=6.

Using the Durbin Watson (DW) to test autocorrelation gives a value of 2.8443 which lies in the Durbin Watson (DW) partition curve within the inconclusive region, hence, concluded that degree of autocorrelation does not exist.

Table 4 above is the regression result derived from the information in table 3. It reveals the effect between business income/reported profit (dependent variable) and depreciation, tax and dividend (independent variables) using current cost accounting. The result of the regression analysis indicates that the coefficient estimates of the regression parameters conformed with our economic expectation as shown in the negative signs of the parameters. This implies that the independent variables which include depreciation, dividend and taxes; negatively influence reported profit which is the dependent variable. This indicates that a reduction on the dependent variable that is; reported profit is caused by an increase in the independent variables.

The R-square; 0.9120 indicates that 91.2% of the sampling variation of the dependent variable is explicable caused by the variables which can be explained while 8.8% cannot be explained. The remaining 8.8% could be resulted from other variables not structured in the model. The R-square value indicates a significant relationship between the dependent and explanatory variables.

The adjusted R-square value is 0.8830. This indicates that the explanatory variable is responsible for about 88% variation in profits, while about 11.7% of the variation is accounted for by the error term.

To test the statistical model significance, F-statistics was applied. The outcome is at 5% significant level, this is due to the fact that F-statistics calculated value of 24.9271 is higher than 4.76 which is the table value at df1=3 and df2=6.

Using the Durbin Watson (DW) to test autocorrelation gives a value of 1.1247 which lies in the Durbin Watson (DW) partition curve within the inconclusive region, hence, concluded that degree of autocorrelation does not exist.

4.3. Test of Hypotheses

Ho: There is no significant difference between the effect of depreciation, tax and dividend on reported profit computed on historical cost theory and current cost theory

H₁: There is significant difference between the effect of depreciation, tax and dividend on reported profit computed on historical cost theory and current cost theory

The result shows that there is a significant difference between the effect of depreciation, tax and dividend on reported profit computed on historical cost theory and current cost theory; therefore, we accept the alternative hypothesis.

4.4. Discussion Of Findings

After a critical examination on the empirical analysis of the duo i.e. profit based on historical cost accounting and that based on current cost accounting, it can be recognized that although both accounting methods have a significant effect on business income, the profit under the historical cost accounting was higher than that of the current cost costing. The implication of this is that most organisations are ignorantly operating at loss. Other issues revealed was that historical cost accounting charges lesser depreciation cost against profit compared to current cost accounting. This outcome corresponds with the works of Mathews and Perera [1996]; Gay [1993] as their analyses revealed that depreciation charged to profit using historical cost are lower if compared to current cost method resulting in overstated reported profit. In addition, tax and dividends paid during the period are questionable. Meeting these obligations based on reported profit derived from historical cost analysis might result in the company paying out of their capital base. This could lead to a critical threat on the company's financial strength. This finding is in line with Tearney [2006] and Paton [2000] stating that any attempt to use only historical cost method in recording transactions in this present period of inflation may lead to reduction in capital and Teemu [1991] confirmed this affirmation.

5.1. Conclusion

The study showed that the operating income of the organizations is significantly influenced by the values charged as either taxes or depreciation, or paid as dividends, in as much as reported profit directly relates to the organisation's operational expenses and the basis of accounting used by the entity also relates directly to its reported profit, the method adopted for measurement of income also

influence the amount computed as depreciation, charged for taxes and stipulate the value of dividend to be paid from reported profit in a given period. It can therefore be concluded that amount calculated as depreciation, charged as tax bill and the dividend paid can significantly affect the operating profit of the entity.

The findings also reveal that that where an organization fails to critically account for inflation or evaluate the current and realizable values of its assets, liability and overall economic transaction it might be overstating the profitability level by charging less estimation of depreciation cost, and also leading to payment of boisterous tax bills and dividend. In the actual sense the reported profit using the historical cost accounting under inflationary period can simply be a jest, mirage or over-estimated, as it might not correlates with the firm's actual performance.

5.2. Recommendations

Based on the findings and conclusion of this study, it is recommended that;

Since inflation has made inadequate; the use of historical cost accounting method as an effective basis of income measurement, companies should embrace the use of inflation accounting methods in preparation of financial statements as it gives them the momentum of reporting assets or liabilities at a current market or realizable value of an arm's length transaction.

Historical cost financial statement can be published alongside the current cost financial statement to be presented to the shareholders and other investors, this will give the firm and all its stakeholders the opportunity to know the true worth of the business before declaring dividends or interests as well as making any investment decisions.

As historical cost analysis overstates reported profit of the entity which can impair on the going concern of the organisation. Companies' profitability level should be evaluated based on the purchasing power of money in order to know the actual worth of the company.

To maintain the capital of the firm, business organisations are urged to carefully consider the variations in profits obtained using both theories as the current cost will provide a better basis for capital maintenance.

The regulatory authorities should enforce current cost financial statement as precondition for filing annual returns. This condition can also be a requirement for listing firms on the stock exchange; this will protect investors' interest and other stakeholders especially during inflation period.

Workshop and seminar should be organized by professional bodies to educate accountants and

managements on the need to adopt inflation accounting methods that would reflect the real value of their transactions as a panacea to ensure their going concern.

IFRS specifies that constant measuring units be used by organizations in hyperinflationary economy in reporting economic events [IAS 29]. It is recommended that firms in developing nations such as Nigeria should adopt the use of inflation accounting methods due to persistent inflation experienced by such countries.

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