International Journal of Trend in Scientific Research and Development (IJTSRD)
Volume 6 Issue 1, November-December 2021 Available Online: www.ijtsrd.com e-ISSN: 2456 – 6470

Related Party Transaction and Performance of Quoted Banks in Nigeria

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ABSTRACT

This study examined the effect of related party transactions on return on total equity of quoted commercial banks in Nigeria. Data for the study were analyzed with descriptive statistics and ordinary least squares (OLS) analysis was used to test the hypothesis using Statistical Package for Social Sciences (SPSS). The findings show that related party transaction has statistical positive relationship on the return on equity of the quoted Nigerian commercial banks. Based on the findings of this study, the researcher recommends that equity shareholders must always ensure that dividend declared are not based on falsified profit especially when related party transactions which has inherent risk of corporate failure are involved.

KEYWORDS: *Related party transactions, profitability and Return on equity and Commercial banks*

How to cite this paper: Okerekeoti, Chinedu U. "Related Party Transaction and Performance of Quoted Banks in Nigeria" Published in International Journal of Trend in Scientific Research and Development (ijtsrd), ISSN: 2456-6470, Volume-6 | Issue-1, December 2021, pp.1034-1041, URL: www.ijtsrd.com/papers/ijtsrd47968.pdf

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INTRODUCTION

The goal of accounting is to provide users with reliable and accurate accounting information about a company's activities so they may make informed decisions. Nonetheless, the accuracy of accounting data presented in financial reports has been questioned, and user confidence has been eroded. This is in relation to the manipulation of financial reports, as shown in well-known incidents of corporate failures and fraud such as Cadbury, Intercontinental Bank, and Oceanic Bank, among others. The goal of these scams is to deceive consumers by presenting a forged report, resulting in a substantial asymmetry of information that impacts decision-making. Related party transactions have been identified as one of the instruments used to commit these scams, exposing the inherent risk involved (umobong, 2017).

A related party transaction is a business transaction between a company and other companies that have an existing business arrangement or investment with the company, such as subsidiaries, associates, joint ventures, affiliates, and so on. Related party transactions are defined by the International Accounting Standard 24 (IAS24) as a transfer of resources, services, or liabilities between a reporting business and a related party, regardless of whether a price is charged. The implication is that a connected party could use these transactions to move assets in and out of the company. Controlling shareholders, subsidiaries, associates, directors, and any other group with a degree of influence over the company (such as affiliates, joint ventures, and close members of the related party's family), according to Pozzoli and Venuti (2014), are all considered "related parties." The IAS 24 is a set of accounting rules and standards that have been designed as an internationally recognised guideline for organizations' financial reporting when related parties are engaged in order to avoid falsification of reports when related parties are used as coverage. Related party income is revenue derived by related party transactions, and it has the potential to effect profitability, as detailed in Fabrizio and Melchiorre's (2015) study "Revenues From Related Parties: A Risk Factor In Italian Listed Company Financial Statements." According to the findings of the study, the intensity of linked party

revenues is higher when a company's profitability and turnover have both decreased. Furthermore, the absence of related party transactions between related parties does not imply that linked parties have no impact on a business.

Over the years, the Nigerian banking industry has seen incidents of business failure that have resulted in bank closures or mergers. Skye bank was recently shut down despite the fiscal and monetary regulations in place to govern and avoid corporate failures in Nigerian institutions. Related party transactions have resulted in incidents of business scandals, according to Gordon and Palia (2004) and Renna and Yanuar (2015) research. As a result, the need for this study, which aims to see if there is a link between related party transactions revenue and group profitability of Nigerian banks, in order to prevent future corporate failures in Nigerian banks caused by a situation where commercial banks show a healthy group profit position in their financial statements while the majority of the revenue is generated by small companies known as subsidiaries.

Furthermore, the majority of empirical research on related party transactions was conducted in other countries, resulting in findings that do not completely fit the Nigerian economy. This is in line with Umobong (2017), who states, "Prior studies on the effect of related party transactions on financial reporting and performance that were recently conducted were mostly conducted in European countries, highlighting a major gap in the literature taking account of the differences that exist in culture, legal system efficiency, and economy between third world and developed countries". As a result, there is a need for research into related party transactions in the Nigerian economy. As a result, the study looked into the impact of related party transactions on the return on equity of Nigeria's publicly traded commercial banks.

Review of Related Literature

Related Party Transaction

According to Corlaciu and Tudor (2011), International Accounting Standard 24 establishes the general reporting framework for related party transactions (IAS 24). Transactions between related parties might take many different forms. Many of them include transactions that occur in the ordinary course of business, such as purchases or sales of goods at market prices. Others, on the other hand, can include large one-time transactions that may be at a fair value on an arm's length basis, or at book value or another sum that differs from market values. "However, the existence of provisions in the standard affords authorities to both workers participating in the preparation of the financial statements, as well as auditors, to reject any suppression of disclosure," according to IAS 24's stated goal. Regulators and other authorities can also use the standard's requirements to investigate and punish any discovered illegality. The International Accounting Standard (IAS) 24 is a disclosure standard. It specifies how related party connections, transactions, and balances should be identified, as well as when and how disclosures should be made. (paragraph 2 of IAS 24). Related party transactions and balances must be disclosed in the individual financial statements of parent firms and subsidiaries, according to the standard.

Subsidiaries and parent firms that submit consolidated financial statements with their individual financial statements are not exempt from disclosing intra-group transactions. There is also no "confidentiality" exception, even if a legal duty of confidentiality is imposed on a corporation. The IASB has indicated that disclosure of related party transactions and balances is critical information for external parties who need to know the extent of support offered by related parties when it comes to intra-group transactions between parents and subsidiaries (IAS 24). Many subsidiaries, for example, rely on their parents for financial support, and those who extend credit to such subsidiaries should be aware of the level of support provided by the parent, or the absence thereof.

The first benefit of related-party transactions, according to the Asia-Pacific Office of the CFA Institute Centre for Financial Market Integrity (2009), is contracting efficiency. Related parties can avoid the stumbling blocks and delays that often accompany contract negotiations with third parties. Related parties may theoretically be able to draft contracts with each other more swiftly than they can with non-related businesses. Dealing with related businesses can help them avoid the delays sometimes faced with third-party suppliers, which is especially beneficial for those in the industry of delivering a variety of services.

Connected transactions, for example, might be a critical component in the development of a vertically integrated business model for a contract manufacturer. These organizations, as well as their clients, see the ability to control inventory and operations without the danger of surprises from unreliable suppliers as a strategic and cost advantage. Strategic feedback is a second potential benefit of related-party transactions. If they represent particular organizations with whom the company does business, people associated with the company may be able to

share important knowledge. A firm with a wide number of suppliers, customers, and advisers may need to appoint people to the board of directors who are aligned with these groups in order to guarantee that the company has the experience it needs to make sound decisions. The convenience of investment is a third benefit of related party transactions. For example, a stock market-listed distressed medium-sized company could be in trouble.

Related Party Revenue and Its Measure

Revenue is the gross inflow of economic advantages during a period originating in the usual course of an entity's business when those inflows result in increases in equity, excluding increases due to contributions from equity participants (IAS 18). Related party revenue is revenue that accrues to an entity as a result of related party transactions.

The intensity of related party revenue will be quantified using the intensity of related party revenue ratio cited in Fabrizio and Melchiorre's (2015) research, which looked at the intensity of related party revenue in relation to profitability and turnover. This is how the ratio is expressed:

$$\text{Related party revenue intensity} = \frac{\text{Related party revenue}}{\text{Operating revenue}} \times \frac{100}{1}$$

Return on Equity

Ordinary shareholders who own a business face all risks, participate in management, and are entitled to all earnings left after outside creditors' claims on the business have been paid. As a result, a company's profitability should be measured in terms of the return to regular shareholders from the perspective of the owner. Return on investment (ROI) A ratio is a measurement of an organization's profitability in terms of return to its owners. This figure shows how much the company has profited from the money invested by its shareholders (either directly or through retained earnings). This ratio is calculated as a percentage of net profit made divided by the owner's equity.

Return on Equity =

$$\frac{\text{Net profit}}{\text{Equity (shareholder's fund)}} \times \frac{100}{1}$$

Empirical Review

The need to gain a better understanding of the relationship between related party transaction revenue and group profitability has resulted in an empirical analysis of literature by a number of scholars who looked at related party transactions from various angles. Fabrizio (2015) looked at linked party revenue as a risk factor for profitability in Italian enterprises. The study's findings reveal that as a company loses profitability and turnover, the intensity of linked party revenues increases. The two variables have a negative correlation, which means they are unrelated. Godsday and Edirin (2016) focused on publicly traded companies in Nigeria, and their research on RPT and financial performance revealed that there is no substantial effect of RPT on financial performance, implying that the two variables are unrelated. Gordon et al (2013) discovered that RPTs are negatively linked with industry-adjusted returns and that worse corporate governance measures are associated with more RPTs. A negative link occurs between industry-adjusted returns and loans to executives and nonexecutive directors, as well as a similar relationship for other types of RPTs with nonexecutive directors. Hu, Shen, and Qiang (2015) conducted an empirical study in Dubai on related party transactions and audit fees for listed businesses. The findings revealed that there is no correlation between RPT and audit fees. Linvani et al. (2010) used a sample of 50 Indonesian publicly traded businesses for the years ending in 2004 and 2005 to investigate the relationship between related party transactions and earnings management. According to the findings, the simple presence of related party transactions in Indonesian companies does not necessarily imply that management is more concerned with earnings management. According to Moataz (2014), earnings management and RPTs have a negative and significant association. This outcome refutes the notion that RPTs are undertaken solely to conceal fraud or the extraction of business assets. The findings also revealed that companies audited by one of the Big 4 audit firms have poorer earnings management. The study also looked into the relationship between RPTs and accounting quality, and found that there is no substantial difference in accounting quality between RPTs and non-RPTs firms. Pozzoli and Venuti (2014) looked into the relationship between RPTs and financial performance of companies, to see if there is a link between these types of transactions and earnings management in Italy. According to the findings of the linked data analysis, related party transactions and financial performance results are unrelated, and there is no indication of a cause-and-effect relationship. As a result, related party transactions are common. Muhrtala et al. (2015) focused their study on the influence of a large number of directors, both executive and non-executive, on RPT. Nonetheless, the presence of many directorships on boards failed to evolve as predictors for related parties' transactions, demonstrating that the number of directors on boards had no meaningful impact on a firm's related parties' transactions. Ezejiofor (2018) assessed how much the

value relevance of financial information has improved in Nigerian manufacturing enterprises since the implementation of International Financial Reporting Standards (IFRS). For the study, an ex-post facto research design was used from 2008 to 2015. With the help of SPSS version 20.0, the data was analyzed and validated using regression analysis and the Chow test statistical methods. The adoption of IFRS has boosted the book value per share, market share price, earnings per share, and cash flow of companies, according to the study. While ownership structure failed to explain the amount of RPTs, Padmini (2013) found that companies with high RPTs related to sales and income reported inferior performance than companies with low RPTs. RPTs were also found to be lower in companies where significant audit firms were statutory auditors. Nestor and Ezechukwu (2017) investigated the impact of cash holding on the financial performance of Nigerian listed insurance firms. The data for the study was acquired from fact books, annual reports, and the accounts of the mentioned insurance companies under review, using an ex-post facto research design using time-series data. With the help of STATA 13 statistical software, the three hypotheses were tested using Pearson coefficient of correlation and multiple regression. Cash holding has a favorable and statistically significant effect on financial performance, according to the findings. According to Ryngaert and Thomas (2012), some related party transactions are harmless and do not indicate opportunistic behavior. These findings imply that the presumption that related party transactions represent a kind of conflict of interest should not be taken for granted, and that generalizations should be made with caution. From 2010 to 2019, Amahalu and Obi (2020) investigated the impact of financial statement quality on investment decisions of listed Deposit Money Banks (DMBs) in Nigeria. Secondary data was acquired from a sample of seven (7) DMBs using an ex-post facto study design. In order to meet the study's aims, inferential statistics such as Pearson correlation and Ordinary Least Square (OLS) regression analysis were used. At a 5% level of return on equity, financial statement verifiability, financial statement timeliness, and financial statement understandability have a considerable favorable effect on listed Deposit Money Banks in Nigeria, according to the findings of this study. In Indonesia, Utama et al (2010) looked at stock market reactions to firms' related party transactions (RPT) announcements. There is no discernible difference in market reaction between RPT and non-RPT releases, according to the research. Furthermore, the study reveals that RPT are more efficient with better transaction disclosure and are regarded as a form of expropriation with higher board share ownership and foreign shareholders as the majority shareholder. Ezejiofor, Nwakoby, and Okoye (2016) examined manufacturing firms' investment decisions to see if they are comparable to commercial banks in Nigeria. The use of an ex-post facto research design was chosen. Financial ratios were utilized to examine the data, and the t-test statistic was performed with the help of SPSS version 20.0. The findings show that there is a significant difference in profitability between manufacturing firms and commercial banks in Nigeria; that there is a significant difference between manufacturing firms and commercial banks in Nigeria; and that there is a significant difference between manufacturing Umobong (2017) investigated related party transactions and business performance for 35% of the population of manufacturing firms listed in the Nigerian economy's food, beverage, and pharmaceutical subsectors. The study found a positive link between RPT and ROA, ROE, and EPS, meaning that higher RPT results in better performance and lower RPT results in worse performance. According to the data, companies are not currently employing RPT to bloat earnings, but rather to improve its performance in conjunction with the efficient transaction theory. Ezejiofor, Nwakoby, and Okoye (2015) investigated the impact of Human Resource Management on the performance of businesses. The data was examined using a five-point Liker's scale in this study, which used a survey research approach. Simple regression analysis was used to examine the hypotheses. Human Resource Management has an impact on the performance of a corporate organization, according to the findings of this study. The thesis of Zuni (2013) made a significant contribution to the literature. It was one of the first studies to look into the nature and scope of related party transactions across six countries in the Asia-Pacific region (Australia, Indonesia, Malaysia, the Philippines, Singapore, and Thailand), and it provided empirical evidence of a link between financial reporting and corruption in a cross-country setting. From 2008 to 2019, Nzekwe, Okoye, and Amahalu (2021) investigated the impact of sustainability reporting on the financial performance of Nigerian quoted industrial goods businesses. This study relied on panel data derived from annual reports and accounts of sample firms for the years 2008 to 2019. The study used an ex-post facto research design. The study's hypotheses were tested using Pearson correlation coefficient, Panel least square regression analysis, Granger causality test, and Hausman test. The findings revealed that environmental, social, and economic reporting are all important.

The majority of empirical research on related party transactions was conducted in other countries, resulting in findings that do not precisely fit the Nigerian economy. This is in line with Umobong (2017), who states, "Prior studies on the effect of related party transactions on financial reporting and performance that were recently conducted were mostly conducted in European countries, highlighting a major gap in the literature taking account of the differences that exist in culture, legal system efficiency, and economy between third world and developed countries". As a result, there is a need for research into related party transactions in the Nigerian economy.

Methodology

The research design used in this study was ex-post facto. Because it is used to analyze historical data and analyzes the effect of one variable on another, the ex-post facto technique was deemed appropriate (dependent and independent variables).

The aggregate listed commercial banks in Nigeria, which comprised the study population, were the focus of this study. The study randomly selected eight (8) banks for this study, and yearly reports from these banks were examined for a period of twelve years (2008-2020).

Data Collection

The primary data collection approach used in this study was secondary data collection. The majority of secondary data was taken from the commercial banks under investigation's annual financial reports.

This method elucidates the link between related party transactions and the profitability of a commercial bank. This was accomplished by utilizing the data that was available.

Method of Data Analysis

Data collected were quantitative in nature and were analyzed with descriptive and the ordinary last squares (OLS) method were used for econometric analysis in the study with aid of Statistical Package for Social Sciences (SPSS).

Model Specification

The functional correlation between the dependent and the independent variables in this study is as follows;

$RPTR_{it} = \beta_0 + \beta_1 ROE_{it} + e_{it}$

Where

RPT = Related party transaction revenue is the independent variable.

ROE = Return on equity as the dependent /explanatory variable

ε is stochastic or error term

$_1$ is the 1th observation

β0= constant

Return on Equity [ROE] =

$$\frac{\text{Net profit}}{\text{Equity}} \times \frac{100}{1}$$

Independent variable

RPTR = Related Party Transaction Revenue [proxied by RPTR]

Related Party Transaction Revenue ratio=

$$\frac{\text{Related party revenue}}{\text{Operating revenue}} \times \frac{100}{1}$$

Decision Rule

If the p-value is less than or equal to 0.05 [5%], we reject the null and accept the alternative hypothesis at 5% level of significance.

Data Analysis

The hypotheses were examined using regression analysis and the Statistical Package for Social Sciences (SPSS) to test the relationship between the dependent and independent variables. Regression analysis with a 95 percent confidence interval was performed to test the hypotheses; the level of significance (a-value) was set at 0.05. (5 percent). If the p-value (calculated r) is smaller than the a-value, reject H0 (Level of significance).

Table 1: Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation	Skewness		Kurtosis	
	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic	Std. Error	Statistic	Std. Error
RPTR	90	-.1716	1.0000	.257658	.3240152	1.558	.254	.791	.503
ROTE	90	-.9309	1.2280	.117734	.1920388	.129	.254	21.730	.503
Valid N (listwise)	90								

Source: SPSS 21 Output, 2021.

Table 1 evaluates the statistical properties of the variables of this study based on the quoted commercial banks in Nigeria; the descriptive analysis of the data collected as shown in table 1 indicates that the average value of the

related party transaction (RPT) sample quoted commercial banks in Nigeria is 25.77 percent (0.257658), implying that the sampled quoted banks on average related party revenue is 25.77 percent with the maximum and minimum v 0.3240152 is the standard deviation.

Finally, the average profitability of the sampled Nigerian banks is 11.77 percent (mean=0.117734), as evaluated by Returns on total equity (ROTE). This indicates that these banks have a Return on Total Equity of 11.77 percent, with a maximum of 1.2280 and a minimum of -.09309, respectively. It differs by 0.1920388 from the sample's mean value of listed Nigerian food and beverage companies.

The Skewness coefficient of the variables ROTE and RPTR in this study was positive, indicating that the distributions are positively skewed and moderately dispersed.

Test of Hypotheses

Ho: There is no significant relationship between related party transaction revenue and return on equity of listed commercial banks in Nigeria.

H_I: There is significant relationship between related party transaction revenue and return on equity of listed commercial banks in Nigeria.

Table 1: Regression Analysis showing relationship between related party transaction revenue and return on total equity of listed commercial banks in Nigeria

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.112	.026		4.286	.000
	RPTR	.024	.063	.040	.375	.708
a. Dependent Variable: ROTE						

Source: SPSS 21 Output, 2021.

Table 2: Model summary of the related party transaction revenue (RPTR) on return on total equity (ROTE).

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.040[a]	.002	-.010	.1929724	.002	.141	1	88	.708	2.086
a. Predictors: (Constant), RPRR										
b. Dependent Variable: ROTER										

Source: SPSS 21 Output, 2021.

Table 1, shows that there is a positive (t-statistics, 0.375) but negligible (p-value 0.708) relationship between related party transaction (RPT) and return on total equity (ROTE) of quoted Nigerian commercial banks based on regression analysis. This means that a 0.040 rise in related party transactions (RPT) will tend to improve the level of return on total equity (ROTE). According to this test, the related party transaction (RPT) has a negligible positive effect on the listed commercial banks' return on total equity (ROTE), hence the null hypothesis (H0) is accepted because the p-value (0.708) is greater than the a-value (0.05).

R2 is the percentage of return on total equity (ROTE) that can be explained by changes in the independent variable, related party transaction, as shown in table 2. (RPT). Adjusted R2 is -.009 in this situation (-0.1 percent). This means that the effect of the independent variable, related party transaction (RPT), could account for about -0.1% of variation in return on total equity (ROTE), while other factors capable of affecting changes in return on total equity (ROTE) of total Nigerian banks could account for the remaining 100%. The Durbin-Watson statistic is also 1.602 in this example. This means that the data series has no autocorrelation.

Conclusion and Recommendations

The primary goal of this research is to determine the impact of related party 3transaction revenue on the group profitability of Nigeria's publicly traded commercial banks.

Using the variables return on total asset, return on capital employed, and return on total equity, the study looked to see if related party transaction revenue has a substantial impact on commercial bank profitability. This was done to see if commercial banks manipulated profits by using related party transaction revenue. Using return on total asset, return on capital employed, and return on total equity, the study found

a favorable association between related party revenue and profitability. The results of the variable return on total asset study were similar to those of Umobong's prior research (2017).

The hypothesis regression analysis result showed a positive but insignificant association between transaction (RPT) and Return on Total Equity (ROTE) of quoted Nigerian commercial banks. This positive effect means that as the number of related party transactions (RPT) rises, so does the amount of Return on Total Equity. This result is in line with Umobong (2017), who discovered a positive but negligible association between RPT and ROTE. Based on the findings of this study, the researcher recommends that equity owners should guarantee that dividends issued are not based on fictitious profit, particularly when related party transactions are involved, which carries a high risk of company failure.

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