COMPARATIVE ANALYSIS OF FAIR VALUE AND HISTORICAL COST ACCOUNTING ON REPORTED PROFIT: A STUDY OF SELECTED MANUFACTURING COMPANIES IN NIGERIA

BESSONG, PETER KEKUNG and   CHARLES, EFFIONG
DEPARTMENT OF ACCOUNTING
FACULTY OF MANAGEMENT SCIENCES
UNIVERSITY OF CALABAR, P.M.B.1115, CALABAR, CROSS RIVER STATE, NIGERIA
Tel: +234 8037079607

ABSTRACT

This study aimed to critically examine the effects of fair value accounting and historical cost accounting on the reported profits. However, since the major objective of any business organization is to make profit and continue in business, what they face in the course of doing their business and the method of accounting they use in reporting their profit may make this noble objective to be unrealistic particularly during inflationary period. Data were collected from both primary and secondary sources and presented and analyzed using ordinary least square. The study revealed that both historical cost and fair-value accounting have significant effect on reported profit. Conclusively, Based on the findings of the study, it is concluded that the amount calculated as depreciation, charged as taxes and paid as dividends greatly influence the operating profit of the company. This simply means that the method of profit measurement will greatly influence the amount charged as taxes, depreciation and dividend on the profit of the company. The study recommended that companies should prepare their financial report using both historical cost and fair-value methods simultaneously. This will allow the companies to know the true financial position of their companies before declaring dividend and other benefits.

Keywords: Current Cost, Depreciation, Dividend, Fair Value, Historical Cost

1.0 Introduction

The basic purpose of financial reporting is to provide information of an economic entity to the user in an economy such as Nigeria, what method of reporting should be used so as to present a true and fair view of the state of affairs of the business? The historical cost principle, which is the traditional reporting method, does not accommodate price changes. Selling price is stated at current price while the cost of assets used in generating the sales are stated at historical cost "acquisition cost". This results in overstated profit leading to overpayment of tax and dividend.

Depreciation is charged based on the acquisition cost of the assets irrespective of the current replacement cost of such assets. The effect of this is overstated profit and understated value of assets which will make replacement difficult.

The usefulness of accounting information about an enterprise increases greatly if it can be compared with similar information about other enterprises and with similar information about the same enterprise for some period or some other point in time (FASB, 1980). Comparability addresses comparing information among different entities while consistency addresses comparing information over time for the same entity. Different firms may use different accounting principles making comparison among firms, even within the industry, difficult at best. Fair Value Accounting (FVA) does not ease the comparability problem and likely exacerbates it. Fair Value Accounting (FVA) also has a significant impact upon consistency. When the market financial assets decline precipitously and the valuation inputs change over night, it is impossible for the information to be consistent.

Fair Value Accounting (FVA) seems to result in a situation where comparability and consistency are more compromised than in the traditional accounting model.

However, since the major objective of any business organization is to make profit and continue in business, what they face in the course of doing their business and the method of accounting they use in reporting their profit may make this noble objective to be unrealistic particularly during inflationary period.

In order to achieve the objectives of this study, the following null hypotheses were formulated to enhance the authentication of the subject matter.

1. H_o: There is no significant effect between depreciation and reported profit using both historical and current costs accounting.

2. H_o: There is no significant effect between tax and reported profit using both historical and current costs accounting.

3. H_o: There is no significant effect between dividend and reported profit using both historical and current costs accounting.

2.0 Literature Review and Theoretical Framework
2.1 Theoretical Framework

The primary function of accounting is the provision of information necessary for the evaluation of past business decision and that business decision consists of current operating profit and realizable cost saving (Edward & Bell, 1991). The link between management and investors is the financial report. Corporation reports should rest upon the assumption that a management is reporting to absent investors who have no independent means of learning how their representative are discharging their stewardship (Turner, 2000).

Solomon (1997) argued that accounting practice of which reporting of profit is fundamental is motivated by and responds to development that enhances the power of accounting to represent neutrally, a given economic reality. This is the basis for the evaluation of the impact of inflation on reported profit. Inflation distorts financial report into which profit is included such that they do not seem to neutrally and accurately represent financial information that is needed for appropriate decision making, policy formulations among many others. Traditionally, financial account prepared by companies includes the balance sheet, the profit and loss account and the statement of sources and application of funds now called cash-flow statement. Presently, companies are also required to prepare the value added statement. The published accounts produced by companies are often designed to serve a number of purposes.

Firstly, they present a snapshot of the company's performance over a period of time, they show the sources of funds and their usages and the viability of the firm in terms of cash/fund usage. Secondly, the company is by statutory obligation compelled to prepare these accounts for the purpose of taxation of the company, ensuring that the company's operation is in cognizance with the law of the land and the need to protect the interest of the members of the public who have investment in such company.

2.1.1 Wealth, Income and Capital Maintenance Theory

Edward (1995) and Friedman (1986) agreed that a change in the purchasing power possessed by an individual represents a change in his or her capacity to engage in transaction. This is true also of business entities. The stock of purchasing power possessed by an entity is commonly referred to as wealth. This relates to the ability of a business entity to acquire assets. An increased capital investment of a firm is certainly a reflection of more wealth accumulation. The wealth in an entity appraised in the light of the stock of purchasing power the firm possesses, is dependent on two factors: a) the general price level and b) the amount of money or money equivalent at its command.

A firm's financial resources are either held as cash, or invested in the acquisition of assets. Changes in the market prices of such assets (either positive or negative) relatively and proportionally affect the capacity of the firm to acquire other goods. Furthermore, the amount of money or its equivalent at the end of the period will have less purchasing power than at the beginning, if the value of money as expressed by the general price level, decreases over a period. Considering the relevance of these two factors to reported final accounts, it is imperative that, in financial reporting, any change in any of them, should be identified and accounted for.

In advancing a definition for Income, Gay (1993) defined Income as the change in purchasing power possessed by the entity between two points in time. Accounting income provides indications of the earning power and future cash flows of a company, which determines its dividend paying ability. Dividend is payable to shareholders as returns on investments and it is paid out of profit after tax and retained earnings, in a proportion that is in tandem with the number of shares held by each shareholder. Dividends so paid, represent part of the firm's earned income that is transferred and distributed to shareholders and it is an indication of the firm's positive cash flow. Accounting income is also of great relevance to tax authorities as it forms the basis for tax assessment. Moreso, it satisfies stewards' purposes as well as wage and price fixing.

According to Slimmings (1994), capital is essentially a financial notion which has reference only to the available finance or the actual money sum employed at the risk of business. Since money is wanted for its general purchasing power, and a certain amount of money or its equivalence represents the capacity of a holder to engage in transaction, it is very logical to say that at least this capacity must be maintained before there can be any surplus or improvement in position. The basic rationale for the concept has been that the capital of the entity should be maintained intact, before distributing dividends to the shareholders, in order to safeguard the interests of creditors.

Different accounting models use different bases for this purpose. For the historical cost model, the capital to be is the nominal capital; for the CCP model and the COCOA model, it is the purchasing power of the initial capital; for the CCA model, it is the physical capital. (Mathews & Perera, 1996).

A current cost profit and loss account includes a number of items not found in the one based on the historical cost convention. The actual number of such differing items will depend on the chosen capital maintenance concept which may be *"Operating Capital Maintenance"* or *"Financial Capital Maintenance"* In Operating Capital Maintenance, the more conventional and convenient way of measuring company's output is by using a proxy of its net operating assets. Net operating assets include company's fixed assets, stock and all monetary assets less all liabilities. So a company will only be deemed to have made profit if it has maintained the level of its net operating assets.

There are four Current Cost Adjustments which might appear in a current cost profit and loss account and which might be regarded as "Converting" a historical cost profit into a current cost profit. The first three are Current Cost Operating Adjustments and the fourth is the Gearing Adjustment. They are as follows:

1. Cost of Sales Adjustment (COSA): This is the difference between current cost of goods sold and the historical cost.
2. Depreciation Adjustment: This is the difference between the depreciation charge for the year based on the current cost of the fixed assets and the charge based on its historical cost.
3. Monetary Working Capital Adjustment (MWCA): Monetary working capital adjustment may be defined as cash plus debtors less current liabilities. In order to operate, most firms need to invest in monetary working capital as well as fixed assets. An increase in prices will mean that the firm will have to increase its investment in monetary working capital and the purpose of the MWCA is to show the additional investment required to cope with the price increase.
4. The Gearing Adjustment: This is the link between the current operating cost and the profit attributable to the equity shareholders.

Financial Capital Maintenance focuses on the shareholders and whether their interest in the firm has increased in "real" terms, that is, after taking account of inflation. This approach deals with both changes in specific prices and inflation and may be described as *real terms current cost system.*

If it is assumed that no capital is introduced or withdrawn during the period, the real term profit can be determined as follows:

i) Measure the shareholders funds at the beginning of the period based on the current cost assets.
ii) Restate that amount in terms of naira purchasing power at the balance sheet date by use of a relevant index of general prices (such as the Retail Price Index (RPI).
iii) Compare the restated amount from (ii) with the shareholders' funds at the end of the year, based on the current cost of assets. If shareholders funds at the end of the period exceed the restated figure for the beginning of the period, a "Profit" has been made; which in ASC handbook is described as "total real gains" (Lewis & Penrill, 1988).

2.1.2 Matching Theory

Paton (2000) described the matching concept as the association of effort and accomplishment. This accounting principle requires companies to use the accrual basis of accounting. The matching principle specifically requires that expenses be matched with revenues. For example, sales commissions' expense should be reported in the period when the sales were made (and not reported in the period when the commissions were paid). Furthermore, the matching principle requires a company to match expenses with related revenues in order to report a company's profitability during a specified time interval. Ideally, the matching is based on a cause and effect relationship: sales cause the cost of goods sold expense and the sales commissions' expense. It follows, therefore, that when expenses

in a period are matched with the revenues generated for the same period, the result is the net income or loss for that period. The matching principle plays a key role in the process of determining periodic accounting profits.

If no cause and effect relationship exists, accountants will show an expense in the accounting period when a cost is used up or has expired. Lastly, if a cost cannot be linked to revenues or to an accounting period, the expense will be recorded immediately. An example of this is Advertising Expense and Research and Development Expense.

In conventional accounting, the notion of matching is used in the sense of matching particular events and their financial magnitudes to numbers representing the monetary amount, regardless of the time at which they occur or the significance of the underlying financial facts. For instance, depreciation based on historical costs may reflect cost levels which prevailed years ago when Naira had a vastly different purchasing power; depending on the inventory method in use, cost of goods sold may represent figure which is quite current or not. In such cases, the current revenue Naira may be matched against expenses which are far from current.

The consistent application of the matching principle requires that all gains made during a period whether realized or not, should be brought into account and matched with all the losses incurred during the period. The income statement for any given period should reflect all revenues properly given accounting recognition, and all costs written off during the period, regardless of whether or not they are the result of operations in that period. Accordingly, it can be argued that first, gains and losses should be taken to include those resulting from the dealing in both short-term and durable inventories; and secondly, any change in the general level of prices during the period should be brought into account (AAA:1986).

2.1.3 Asset Theory

By way of a simple and direct definition, Asset is any object, tangible or intangible, that is of value to its possessor, which can be consumed, appreciated or traded-off overtime. Under the U.S Generally Accepted Accounting Principles (U.S GAAP) as is the case with that of other Countries, assets are generally recorded and carried on their historical cost basis. Historical cost is the actual purchase price plus incidental costs incurred in getting the fixed assets in a condition and position ready for initial use/commercial production. (Weirs, 2005)

A practical effect of valuing an asset at its historical cost can be seen in an instance where a plot of land that was probably bought for ₦120,000 by a firm, some 20 years back, but is perhaps worth at present ₦1,000,000, will still be recorded in the balance sheet of the firm at its historic cost of ₦120,000; and not the current higher value. According to Tearney (2004), the historical cost principle is used because of its reliability and freedom from bias, when compared to their fair market value principle.

Though it may not be difficult to determine with relative exactness, the historical cost of an asset that the amount paid for its acquisition was properly and specifically recorded, this in practice may not always be the case. Sometimes, difficulties may arise in determining the historical cost of some kinds of assets, such as trading stock, whether such stocks should be valued on the basis of *First In First Out* (FIFO), *Last In First Out* (LIFO), *Average, etc.* The problem is even more acute when trading stock involves work-in-progress and unfinished goods, as the question of the extent to which overheads should be apportioned to the stock figure, must be considered. Similar problem arises when determining the cost of fixed assets constructed by the firm for its own use. In some other instances, there is the great challenge of determining what should be recorded and maintained as the historical cost of an asset that was acquired by a firm through a barter system, that is, in exchange for another asset. In such instances, it may be necessary to estimate the historical cost of the assets acquired. This is usually done by reference to the amount that would have been realized had the assets which had been given in exchange, been sold for cash. The historical cost of assets purchased together is also difficult to determine; for example, where a company purchases the net assets of another company. For accounting purposes, it is necessary to determine the historical cost of the individual assets and liabilities which have been acquired and this involves an allocation of the global price to the individual assets and liabilities which are separately identified in the accounting system. Any balancing figure represents the amount paid for all assets and liabilities not separately identified in the accounting system and are described as goodwill. If an asset has been received in consideration of issuing shares or bonds, historical cost is recorded at fair market value of shares/bonds. For example, if a machinery is bought in return of 1,000 shares, which have a market value of ₦12 each at that time, then the historical cost of that machine is ₦120,000. Any subsequent change in the value of those shares is accounted for, separately. If a group of assets are purchased for a single lump sum, the cost paid is allocated among various assets on the basis of their market value. If an asset has been received for another non monetary asset, historical cost is recorded as the fair market value of the asset given up or the asset acquired, whichever is more evident.

It should be as opined by Richard (1996), that costs incurred to improve an asset should be capitalized (that is, added to the historical cost) whereas expenditure that simply maintains a given level of service, should be treated as ordinary expense; and the historical cost of an asset which is taken to be the original acquisition cost is adjusted to account for changes in the value or purchasing power of money, between the date of acquisition and the valuation date.

2.1.4 Depreciation Theory

This theory according to Teemu (1991) states that depreciation should be based upon the historical cost of an asset except that where an asset has been revalued, subsequent depreciation should be based on the revalued amount.

2.1.5 Consistency Theory

This theory according to Igben (2004) states that, when a company selects a method it should continue (unless conditions warrant a change) to use that method in subsequent periods so that a comparison of accounting figures over time is meaningful. The theory ensures that the accounting treatment of like items is consistent taking one accounting period with another.

The application of this concept requires that if, for example, the firm chooses to depreciate its motor vehicles on straight line basis, it should continue to do so in subsequent periods. It would not be proper to use straight line method in one period, then reducing balance method in the next period, and sum-of the-digits method in the period after that such that meaningful comparisons of accounting figures could be made overtime.

Another aspect of consistency is that, having chosen to depreciate motor vehicles on straight line basis all motor vehicles owned by the firm – the Mercedes "S" class used by chairman, the delivery van used by the sales staff, motorcycles used by dispatch clerks etc should be depreciated on this basis.

2.2   Financial Reporting

According to Williams (1977), financial reporting is the means of conveying to management and interested outsiders, a concise picture of the profitability and financial position of the business. He concluded that, it is made up of two statements, balance sheet and income statement. Pandy (1988), on the other hand states that financial report is synonymous with financial statement and is a statement which summarizes the information of the firms, financial situation to owners, creditors and the general public. Statement of Accounting Standard (SAS) 2 recorded that, financial statements consist of the balance sheet, profit and loss account or income statement, statement of source and application of funds, value added statement note to the account and five years historical financial summary.

From the researcher's point of view, financial reporting-financial statement are the means by which investors, government, creditors, competitors, suppliers customers and the general public who have no access to management accounts, evaluate the performance of an enterprise. They are the communication link between the management and the members of the public.

2.2.1   Objectives of Financial Statement

According to the Trueblood report (1973) (in Glautier & Underdown, 1986) the objectives of financial reporting by business enterprises are as follows;
1.   To provide information useful for making economic decision
2.   To serve primarily those users who have limited authority, ability or resources to obtain information and who rely on financial statement as either principal source of information about an enterprise economic activity.
3.   To provide information useful to investors and creditors for predicting, comparing and evaluating potential cash flow to them in terms of amount, timing and related uncertainty.
4.   To provide users with information for predicting comparing and evaluating enterprise earning power.
5.   To supply information useful in judging management's ability to utilize enterprise resources effectively in achieving the primary enterprise goal.
6.   To provide factual and interpretive information about transactions and other events which is useful for predicting comparing and evaluating enterprise earning power.
7.   To provide information useful for the predictive process. Financial forecasts should be provided when they will enhance the reliability of user's predictions.

8.   For governmental and not-for-profit organization, an objective is to provide information useful for evaluating the effectiveness of the management of resources in achieving the goals of the organizations

9.   To report on those activities of the enterprise affecting society, which can be determined and described or measured and which are important to the role of the enterprise in its social environment.

2.2.2 Criticism of Financial Reporting
        Financial practice has been the subject of much criticism on the following grounds

a)   Lack of uniformity in accounting practice made it difficult for the comparison of the financial report of different companies

b)   Multiplication of accounting practice made it possible for management to select alternative presentations of the financial results which allowed earning to be manipulated and made it possible to conceal economic realities.

c)   Changes in the value of money added to the difficulty of comparing the financial statement of different companies in a meaningful manner and added a new dimension to the problem of financial reporting (Glautier & Underdown, 1986).

2.3   *Approaches to financial reporting in accounting literature*
        There are many approaches to financial reporting, these are:
(a)   Historical Cost Accounting (HCA)
(b)   Current Cost Accounting (CCA)
(c)   Replacement Cost Account (RCA)
(d)   Current Purchasing Power Accounting (CPPA)

2.3.1   Historical Cost Accounting (HCA)
        This method is used in current accounting practice. It is the traditional method of recording assets at the original cost. The historical cost accounting is on the assumption that money is a stable unit of measurement. According to Meigs (1984), using this method, profit is determined by comparing sales revenue with the historical cost of the asset sold. Thus in income determination, accountants assumed that a business is well off when it has recovered its original money investment and that it is better off whenever it recovers more than the original sum of money invested in any given asset. The fact that historical cost accounting is based on historical cost, Jennings (1986), states that it is inadequate for accounting during price level changes. Supporting his assertions, he states that financial statements prepared with the historical cost concept have always been apparently defective to the extent that:

a.   It fails to reflect the effect of changing price level

b.   Assets are disclosed in the balance sheet at unrealistic values

c.   The profit and loss account does not bear proper charges particularly for depreciation and cost of material consumed.

        Furthermore, he stated that the situation has been aggravated through the 1970s by the accelerated rate of inflation. The products and services have been under-costed, producing, fictitiously high (illusionary) paper profit. This illusion created Leads Company's management into wrong decision of paying high dividends, wages and corporate tax out of capital. Mergs *et al.,* (1984), sharing the view with Jennings stated that when the general price level is rising rapidly, the HCA may significantly understate the current economic value of the resources being consumed.

        Simon (1987) in supporting the position of Jennings is of the firm belief that the misleading result of HCA profit which leads to over payment of taxes, dividends and wages during up-ward change in price (i.e. inflation) have made United Kingdom companies not to use the historical accounting in reporting assets. To further prove the inadequacies of the HCA during the period of changing prices, Farmer (1985) also reiterated the position of the accounting standard committee that:

a)   HCA information is not enough

b)   Reports are distorted if current revenues are matched with historical cost

c)   Balance sheet value may be unrealistic

        Barry (1980) also stated that the reliance on the HCA during inflation has been subjected to a number of criticisms. Among these are:

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

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

c.   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.

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

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

He stated further that in view of the various weaknesses of HCA, several solutions were proposed especially in the United Kingdom and United States all culminating in SSAP 16, issued in March 1980 on current cost accounting as preceded by many study groups and their reports.

Although HCA has been criticized, it is not absolutely bad. Its failure in the present times has been as a result of continued rate of inflation in our economy. According to Hendriksen (1982) and Millichamp (1989), HCA possesses attributes such as simplicity, comparability, objectivity, verifiability and measurability.

Anao (1989) noted that the important foundation of financial accounting is historical cost convention. The purpose of this convention is that all accounting entries should be made, and the resultant accounting factors measured on the basis of values which were established at the time of the initial transaction. The principle, he said is believed to have the advantage that it keeps accounting measurement objective and verifiable. He went further to state that despite this, however, a certain undesirable characteristic is associated with historical cost convention namely the fact that in period of fluctuating price level, value derived on the historical cost principle may have no relevance to the actual value (of assets or revenues) as at the material time of reporting. The fact that the monetary unit which is the basis of historical cost measurement has no stable value overtime, owing to the incidence of inflation (or in the opposite case, deflation) , is a major reason why conventionally prepared account may not give a realistic picture. The extremely high rate of inflation (running sometimes into double or triple digits) experienced by most world economies during the last two decades, as well as the accelerated pace of technological development witnessed in certain industries, have the combined effect of altering economic values so rapidly that the conventionally prepared accounts no longer present a satisfactory picture of the operating result or the financial condition of the firm. Accountants are therefore, constantly under pressure from users of accounting information to present financial statement which takes adequate account of changes in price level.

2.3.2   Current Cost Accounting (CCA)

This is an approach to financial reporting whereby profits are measured by comparing revenue with the current replacement cost of the assets consumed in the earning process. The logic of this approach lies in the concept of the going concern. It recognizes in the income statement, the cost which a going concern actually has to pay to replace its expiring assets (Meigs *et al.,* 1984). They went on to say that the profit figure resulting from CCA closely parallels the maximum amount which a business can distribute to its owners and still be able to maintain the present size and scale of its operations.

Glautier and Underdown (1986), in sharing the same view with Meigs (1984) stated that CCA 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. They went further to state that CCA is a modification of historical cost profit to arrive at the surplus after allowing for the impact of price changes on the funds needed to continue the existing business and to maintain its operating capacity, whether financed by share capital or borrowing. But Meigs (1984), stated that CCA represents a departure from the historical cost concept. Furthermore, they stated that, the term "current cost" usually refers to the current replacement cost of assets and in current cost, income statement; expenses are stated at the estimated cost to replace the specific asset sold or used up. Thus, current cost accounting involves estimates of current market value rather than adjustment to historical cost for changes in the general price level. Supporting the position of Meigs and Hendriken (1982) which states that CCA is a method of accounting that reflects prices that would need to be paid, for an asset or its uses, at the balance sheet date or the date of the use or sale, if the assets were already owned. He stated further that, for inventories, current cost is the current acquisition price of the merchandize, or the current cost to produce it. And for plant, equipment, and other property, the best measure of current cost is the use of asset prices of similar conditions and of the same age as the assets owned.

Current cost accounting is therefore a valuation concept which combines the concepts of replacement cost and net realizable value in determining whether selling (existing) price should be used for the purpose of establishing the value of an asset to the business. In further discussions on valuation based on CCA in a competitive market with many buyers and sellers, the price of an asset in this market may reasonably be taken to reflect the current value of asset, if it is in expectation of other firms. Where there is no market for used assets the CCA concept recommends

the approximation of the current cost of an identical new item purchased in current established market, less accumulated depreciation for the period, equal to the age of the asset in use (Hendriksen, 1982). Thus, CCA tends to reflect cost and value to a more realistic figure, relevant for decisions during the period of price level changes.

In general, the advantages of CCA system are that, it overcomes the defect of historical cost system in that, being a current value system accounting, its aim is to represent as far as possible, the commercial reality of the situation to which it refers. Jennings (1986), in specific terms stated the advantages of CCA as:

i. Current costs are matched with current revenue for depreciation and calculated on the value to the business of the assets concerned. In majority of cases, such value is the net current replacement cost, and cost of sales is calculated on actual or assumed date-of-sale cost prices.

ii. The balance sheet shows assets at their value to the business.

iii. As a result of i and ii, users of accounts have available more realistic information on cost, profit and loss, asset value and the return on capital and on assets

iv. The system identifies profits and losses arising from business operations separately from those arising from price level changes.

v. Current basic figures lead to better quality long term and short term decisions.

Hendriksen (1982) in expressing the advantages of CCA stated that:

1. CCA represents the amount the firm would pay currently to obtain the asset or its services, therefore representing the best measure of the value of the input being matched against current revenue for predictive purposes.

2. CCA permits the identification of holding gains and losses, thereby reflecting the result of assets value and management decisions.

3. CCA represent the value of assets to the firm, if the firm is continuing to acquire such assets, and if value has not been added by the enterprise to the assets.

4. The summation of assets expressed in current terms is more meaningful than the addition of historical cost incurred at different times.

5. It permits the reporting of current operating profit useful in predicting future cash flow.

The current cost accounting, although very promising, is not without a hitch. Certain aspects of CCA principle give grounds for doubts as to whether the lofty advantages expected of it are in reality, achievable.

The consultative committee of the accountancy bodies in the United Kingdom and Ireland (CCAB) found the Sandilands reports unacceptable on the grounds that the CCA did not take account of all aspects in inflation. The CCAB puts its case in the following terms; the aspects of inflation which the CCA does not deal with at all or does not deal adequately with are:

a. The decrease in value of monetary assets

b. The decrease in value of obligation represented by monetary liabilities.

c. The whole effect of inflation on the value of the proprietor's interest in the company or other organization concerned, irrespective of whether that interest is represented by non-monetary or monetary assets.

d. The description of the incremental difference between an asset's original cost and its value to the business as a "holding gain" is potentially misleading as the whole or part of the gain will be the result not of a real gain in wealth, but of a decrease in the value of money.

e. The problem of making valid comparisons over a period of time when the unit of measurement is unstable.

Anao (1989) stated that current cost or value approach seeks to value all assets and inputs consumed in the process of generating income on the basis of their "current" value at the time of consumption or realization. The expected net result is the figure of net income which is stripped of any windfall element (holding gain) and thus reflect the pure earnings capacity of the firm and also, of a net asset figure which reflects as closely as possible, the current valuation of the firm's component assets, he argued that CCA is not simply an inflation accounting technique but rather a technique for obtaining accounting data that reflect current values. Although CCA seeks to make accounting information more up to date and relevant for business decisions, certain practical difficulties still tend to hinder the achievement of ideal results. He added that, the most critical problem, which is created by CCA, is the increased difficulty in achieving the determining net realization cost (NRC), net realization value (NRV), and the expected value (EV) in respect of each asset. CCA is based on values, which are as a result of estimates, and there is the difficulty in determining the accurate contribution made by each asset to an income, which results from joint use.

On the whole, the concept of capital maintenance is more relevant to the operations of a business than the general purchase power concepts. Therefore, if a choice has to be made between CCA and the current purchasing power accounting, CCA should be adopted (Glautier & Underdown 1986).

2.3.3   Replacement Cost Accounting (RCA)

This is the method which permits the matching of current input values with the current revenues in the income statement, and also the monetary value assigned to stock at the end of the period represents a current cost (Bull, 1984). According to Glautier and Underdown (1986), the basic concept underlying replacement cost accounting is that the firm is a going concern, which is continually replacing its assets. Therefore, the cost of consuming such assets in the profit generation process should be equivalent to the cost of their replacement. It is therefore concerned with the manner in which price changes affect individual firm. It focuses on the specific commodities and assets employed by the firm, by taking into account changes in the price of such commodities and assets reflected in specific price indices or price indices of group of similar commodities and assets.

Replacement cost accounting is addressed to the concept of capital maintenance, interpreted as maintaining the operating capacity of the firm and involves:

1.   Calculating current operating profit by which the current cost of resources exhausted in earning those revenues.
2.   Calculating holding gain and losses.
3.   Presenting the balance sheet in current value terms.

Glautier and Underdown (1986) listed the following as the advantages of replacement cost accounting

a.   It provides more detailed information than the accounting profit concepts for the purpose of evaluating the result of activities.
b.   RCA indicates whether the sale proceeds are sufficient to cover the cost of the resources sold, that is, whether the activity of selling itself, is efficient.
c.   Where the goods sold are manufactured by firm, current operating profit indicates whether the manufacturing proceed is profitable, for input factors of production are valued at their current replacement cost.
d.   From a long-term point of view, it affords a means of evaluating the firm as a going concern.

They went further to state that the application of replacement cost values attempt to reflect economic reality by maintaining the value of the asset balances in line with changes in the value of money and changes in the specific value of the assets concerned. According to them, replacement cost profit is more relevant to investors than accounting profit for the purpose of decision making; their position is based on the fact that RCA provides for the following:

1.   It provides for the maintenance of the service potential of the capital by charging against revenue the cost of replacing the assets exhausted in earning revenue.
2.   An important distinction is made between operating profit and holding gains, therefore allowing investors to appraise the firm as a going concern
3.   It recognizes changes in the value of assets since they are related to current market prices.

For these reasons, investors are provided with information, which is more relevant than accounting profit for evaluating the business, and they are placed in a better position to predict the future. By providing more accurate valuation of assets in use, replacement cost accounting is likely to lead to a more efficient allocation of financial resources than that afforded by conventional accounting methods.

Although replacement cost accounting has the above advantages, Glautier and Underdown (1986) stated that, RCA reflects a relatively static situation and does not inform investors about the economic sacrifice made in holding resources in their current form and that the present value of future cash flows associated with the holding of assets is the most relevant concept of value from the point of view of investors. Backward holding concepts, such as historical cost and replacement cost value are poor surrogates as predictors of future cash flows.

Anao (1978) noted that RCA departs radically from historical cost concepts in assuming that the best measure of values and of costs is what the goods or assets would cost at the present time, if they have to be replaced in the present condition. Thus, income is what is left of the revenues after deducting from them all costs (including depreciation of fixed assets and inventories) valued at their replacement costs, and the net asset of the business is the

surplus of assets over liabilities valued on the same basis. He stated that, this method has advantage because they permit a notion of income and net assets which approximate to their current value.

2.3.4   Current Purchasing Power Accounting (CPPA)

In 1974, the professional accounting bodies in the United Kingdom recommended that a supplementary statement should be attached to the financial reports of companies showing the conversion of the figures in the financial reports in terms of their current purchasing power (CPP) at the closing day of the accounting period. They recommended that the retail price index (RPI) should be used to effect the conversion of historical cost value into current purchasing power equipment.

Under the CPPA, assets, liabilities, income and expenditure are measured in terms of their current purchasing power at the balance sheet date. Profit is arrived at after allowing for the maintenance of the purchasing power of the shareholder equity at the beginning of the accounting year.

Anao (1987) and Blake (1959) are of the view that, CPPA is out to solve the defects in historical cost accounting methods by using a unit of "constant purchasing power" in the place of the monetary units as a basis for accounting measurement.

Historical cost accounting is based essentially on the money amount maintenance concept. Such a concept asserts that, all funds available to the firm in excess of the original contribution of funds by shareholder make the firm better off. High level of inflation experienced in recent years has undermined the validity of this assertion. CPP accounting attempts to deal with this problem by adjusting historical cost measurements for the effects of inflation as a result, the purchasing power held by the firm is maintained. The profit which results from CPP adjustments may be defined as those gains arising during the accounting period which may be distributed to shareholders, so that the purchasing power of the shareholders' interest in the company is the same at the end of the year as it was at the beginning. (Glautier & Underdown, 1986:266). Although CPP accounting is to restate historical cost in terms of current purchasing power, it is not without its limitation.

Statement of Standard Accounting Principle (SSAP 7) recommended that companies should continue to publish accounts on historical cost basis but that in addition, a supplementary statement should be presented showing the effect of converting conventional account into pounds (Naira) of current purchasing power. The Sandiland reports ruled out CPP accounting because it did not like the idea of two set of accounts or the use of different measurement units. According to the Sandiland reports, users of financial report would be confused. Another objection to CPP accounting is raised by some authorities who believe that there is no such thing as generalized purchasing power (Gynther, 1974 in Glautier & Underdown, 1986). Raising argument in favour of the position of Gynther, Glautier and Underdown, stated that organization and the people do not see themselves as holding general purchasing power when they hold money, rather, they see themselves as holding specific purchasing power in respect of those relatively few items, which they wish to purchase. Hence, the purchasing power of money should be related to those items on which these adjustments are based and not one which maintains the service potential of capital. Therefore, adjusting financial data for the effect of inflation is not the same as reporting current values.

Despite the criticism leveled against CPPA, Glautier and Underdown (1986) are of the opinion that price level adjustment are verifiable by reference to the index used to measure changes in the purchasing power of money and result in alteration of historical cost measurements which are themselves objectives. Therefore, both criteria of objectivity and verifiability are satisfied in CPP accounting.

According to Beredugo (2007), the current purchasing power was developed to meet the criticism of historic cost accounting, the method aims at eliminating inflationary gain shown by historic cost accounts and arising from the fall in the value of money, by valuing a company's net asset at the beginning and end of the year in terms of purchasing power at the end of the year. The increase or decrease in the year of the net asset now shown at constant values, which represents the real reported profit or loss in terms of purchasing power at the end of the year. Purchasing power was assumed to move in line with the retail price index.

There is a high degree of objectivity required for reported profit valuation using the C.P.P approach as it does not depart in principle from historical cost based measurement. Price level adjustments are verifiable by reference to the index used to measure changes in the purchasing power of money, and results in alteration to historical cost measurements, which are themselves objectives. Therefore, both criteria of objectivity and verifiability are satisfied in CPP accounting (Ajayi, 1987).

2.4.   *Fair Value Accounting Standards (FVAS)*

In 2006, the Financial Accounting Standard Board (FASB) issued statement of financial accounting standard No 157(SFAS 157) to establish fair value accounting standard under United States generally accepted accounting principles (US GAAP). In 2009, FASB recodified its accounting standards and SFAS 157 was included under topic 820 of the Accounting Standard Codification (ASC 820).

Under ASC 820, US GAAP requires that fair value measurement be recognized in the financial statement for certain financial statement elements. The recognition process requires adjustments to carrying amount of assets or liabilities which results in the recognition of unrealized gains and losses. ASC 820 (ASC 820-10-35-2, originally SFAS 157, para. 5) provides a single definition for fair value as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date". Thus, ASC 820 defines fair value as an "exit price". ASC 820 also established a framework for measuring fair value and requires enhanced disclosures regarding fair value measurement. ASC 820 does not require any new fair value measurement, but it does standardize measurement and disclosure practices (Grant, 2008).

The main purpose of ASC 820 was to increase consistency and comparability in fair value measurement. Thus, ASC 820 (FASB, 2006) prescribes a framework for performing fair value measurements using three-tiered hierarchy of inputs (Grant, 2008).

Level 1, inputs are observable inputs based upon quoted market prices for identical assets and liabilities in active markets.

Level 2, input are quoted price from sources other than level 1 which are observable either directly or indirectly, such as an interest rate swap which utilizes observable data points like the yield on treasury bonds. A good example of level 2 inputs is provided in a case written by Gore and Herz (2010: 59) in this case, estimating the fair value of the properties in the mountain division of the snowy Rudge Ski Resort requires use of a market multiple, based upon the sales revenue of comparable properties that were sold during the year. Level 1 and level 2 inputs are considered mark-to-market methods.

Level 3 inputs are unobservable assumptions, such as an entity's internal valuation model, that incorporates management assumptions that cannot be corroborated with observable market data. Thus, the use of level 3 inputs is sometimes referred to as "mark-to-model" accounting (King, 2006) and it is used when observable inputs are not available (FASB 2006). It is interesting to note that at the time of issuance of SFAS 157, textbooks depicted level 3 inputs as consisting of present value computation of level 3 inputs provide fair value prices that are entirely dependent upon management's assumptions and therefore less neutral than level 1 and level 2 inputs.

Recently, FASB and the International Accounting Standard Board (IASB) agreed that ASC 820 should be amended to reflect FASB's decision that the "highest and best use" concepts should apply only to measuring the fair value of non-financial assets; to add guidance for determining premiums and discounts in a fair value measurement.

2.5 Current Cost Profit and Adjustment

Current cost profit is determined in two stages. At the first stage, current cost operating profit is aimed at and represents the surplus contributed by the ordinary activities of the business, before interest and taxation but after allowing for changes on the funds needed to continue the existing business and to maintain its operating capital. At the second stage, that part of the current cost profit attributable to shareholders in ascertained by taking cognizance of the way the business is financed.

At the first stage, historical cost operating profit is converted to a current cost basis by the application of three main adjustments for

- Depreciation
- Cost of sale
- Monetary working capital and secondary adjustment for
- Fixed asset disposals

The second stage involves the application of a gearing adjustment to the current cost operating profit to convert it to a figure of current cost profit attributed to shareholders.

The purpose of the adjustments is to make allowance for the impact of price charges on the funds needed to maintain the net operating assets of the business. The depreciation adjustment is the difference between the proportion of the value to the business of the fixed assets consumed and depreciation calculated on the historical cost basis.

The cost of sale adjustment is the difference between the value to the business of stock consumed in the period and its cost calculated on the historical basis. The monetary working capital adjustment is the variation in finance needed for monetary working capital purposes as a result of changes in the input of goods and services used

and financed by the business (monetary working capital is defined as trade debtors prepayment trade bills receivables and stocks not subject to a cost of sale adjustment, less the aggregate of trade creditors accruals and trade bill payable to activities. Items of capital nature are excluded).

Together, the cost of sales and monetary working capital adjustments allow for the impact of price change on the total amount of working capital used by the business in day to day operation.

The fixed asset disposals adjustment is the difference between the historical cost and the current cost value to the business of the gearing adjustment is the proceeds of disposal in each case. The cost adjustments are abated by an amount representing that proportion of the adjustments financed by borrowing.

2.6 Impact of inflation on capital maintenance

In accounting theory, a person's capital is increased by the amount of his periodic income, which he has not consumed. Financial accounting procedure affects this transfer by crediting the net profit to the capital account and if his level of consumption or drawing is less than that profit, the capital is increased by the differences. In the case of companies dividend are analogous to drawings and retained profit is added to the total of the shareholder equity.

One of the important implications of profit measurement in the case of companies lies in calculating what may be safely distributed as dividends. Investors are concerned with maintaining the value of their capital (Glautier & Underdown, 1986).

As a result of stable monetary assumption, however, a strong argument may be made that much of the corporate profit today is an illusion. The argument has been on the fact that, when the general price level is rising rapidly, historical cost may significantly understate the current economic value of the resources being consumed if costs and expenses are understated, it follows that reported profit are overstated (Meigs et al, 1984). They went further to say that when the impact of inflation is not recognized in accounting measurement of income, the following board consequences appear to follow.

(1) Corporate liquidity (debt paying ability) many fall so low as to bring economic crises
(2) Since we allocate economic resources in large part on the basis of financial statement, poor allocation may be the end consequences of ignoring inflation in our financial reports.
(3) The over statement of profit may lead to an unrecognized failure to maintain reasonable rates of capital formation.

Pizzey (1980) argued that the conventional accounting (historical cost) protects the money capital of the business but fails to show how that money capital is being eroded in items of purchasing power during the period of inflation. He based his argument on the fact that historical cost accounting will cause profit to be overstated while the capital employed as shown by the balance sheet will be understated, so that the use of the ratio of net profit to capital as a measure of managerial efficiency is impaired.

If a company pays out a high proportion of its profit as dividend and in the profit is overstated because historical computed at current prices, Pizzey (1980) and Meigs et al (1984) assert that there will be a danger that dividend could be paid out of capital if the dividend exceeds the amount of the real profit.

Ogundele (1981) noted that major advocate in accounting convention is that of basing depreciation upon the replacement rather than historical (original) cost. He went further to state that the question generally asked on accounting for fixed assets and depreciation charge, was "can something be done to incorporate the changes in the purchasing power of money" in the income statement? He reiterated that several suggestions for theory and practice were made, namely:

(1) Appropriate income to take care of asset replacements
(2) Handle the situation by supplementary data that will indicate the effects of the price level changes.
(3) Base depreciation changes on replacement value (costs) of asset.
(4) Restate assets periodically in terms of current price (provided it is worked out with best safeguard).
(5) One of the methods that was considered, as most workable situation is the process of adjustment for price level changes by means of carefully constructed price indexes. As such the costs of utilizing long term facilities are placed on current bases and can be mad e reasonably comparable to the remaining charges in the income statement.

He concluded by stating that a department from conventional cost basis by modification of generally accepted accounting principles in order to eliminate illusionary gain and losses caused by inflation (deflation) is advocated.

Anao (1989) affirming the position of Ogundele, stated that failure to acknowledge the effect of changing price levels in the accounts will generally lead to a distortion of specific factors which many types of decision are usually

based. The resultant decisions may therefore be misled to the extent of any distortion contained in the accounts. Two major factors disclosed by corporate account, profit and net assets are usually quite seriously affected. When there is a rise in general price level. A situation referred to as inflation, the monetary values of most goods tend to rise. The higher the rate of inflation the higher will values also tend to rise on the average. This means, in the first instance, that the assets held by the firm now worth more in current monetary term, than the value stated for them in the accounts. This understatement of set values implies that an unwary investor, relying on the published corporate accounts, would tend to undervalue the share's worth and subsequently the investment.

3.0 Methodology

An attempt was be made in this study to appraise the effect of fair value and historical cost accounting on the reported profit. The research design adopted for the study is descriptive design. This choice of the cross sectional research design is because the data was collected at a particular point in time (2010) from the sampled company.

The population of this study comprised all the 48 quoted manufacturing firms in Nigerian first tier securities market and whose shares were traded on the floor of the Nigerian Stock Exchange (NSE). These firms were considered appropriate population for the study because they were statutorily required to submit their published financial statements to the Securities and Exchange Commission (SEC). Therefore financial statements published to the Nigerian public were validated by the acceptance of such by the SEC as the singular most authoritative financial medium which had consistently published financial information of Nigerian firms for over 15 years and had been closely monitored and financial reporting trends in the Nigerian financial sub-sector (like share index, market capitalization, price gainers/losers, trade volume, total transactions and total deals). The financial statements of these companies were considered the most viable reliable measurement yardstick of the financial strength and operational capabilities of the companies.

Ten (10) of the manufacturing companies were randomly selected from the study population of 48. According to Balsely and Clover (1988), it is common in research studies to use 10 percent sample size, because sample size of 10 percent of the universe has been proved to be more than adequate in research projects. Ogolo (1996) corroborates this when he posited that where a population is known, at least 10 percent of it constitutes a researchable sample. For this study ten manufacturing companies where selected amounting to 20.83% of the universe.

In view of the researcher's inability to reach out to the entire population, and in order to gain the advantages of an in-depth study and effective coverage, samples were drawn using stratified random sampling from different manufacturing sectors in Nigeria. To do this, the names of the manufacturing companies were each written on pieces of papers and placed in a basket. Draws were then randomly made and the companies on the picked pieces of papers were then used for as the samples. The data collected for this study were both primary and secondary data.

3.1 Model Specification

In analyzing the study, the multiple regression technique was adopted because it measured the relationship between the dependent and the independent variables.

In order to test the hypotheses, the study adopted Teemu (1991) Gay (1993); Mathews and Perera (1996); Paton (2000); and Tearney (2004) models where the variables were built into as follows:

Model 1: RP_{HC} = f (DEP, TAX, DIV)
Model 2: RP_{FV} = f (DEP, TAX, DIV)
The above models are statistically stated as thus:

$$RPHC = b_0 + b_1 DEP + b_2 TAX + b_3 DIV + e_i \text{-------------- 1}$$
$$RPFV = b_0 + b_1 DEP + b_2 TAX + b_3 DIV + e_i \text{-------------- 2}$$

WHERE:
RPHC   = Reported Profit at Historical Cost
RPFV   = Reported Profit at Fair Value
DEP   = Depreciation
TAX   = Taxes
DIV   = Dividend
b_0 = Unknown constant to be estimated
$b_1 - b_2$ = Unknown coefficients to be estimated
e_i = Stochastic error term
$b_0, b_1, b_2 \geq 0$

4.0 Data Analysis

Table 1 shows the regression results of the effect between the dependent variable reported profit at historical cost accounting and the independent variables namely; depreciation (DEP), taxes (TAX) and dividend (DIV). The regression results showed that the estimated coefficients of the regression parameters have negative signs and thus conform to our economic a-priori expectation.

The implication of these signs is that the dependent variable, reported profit is negatively influenced by depreciation (DEP), taxes (TAX) and dividend (DIV). This means that an increase in the independent variables will bring about a decrease in the dependent variable, reported profit.

The coefficient of determination, R-square of 0.967 implied that 96.7% of the sample variation in the dependent variable profitability is explained or caused by the explanatory variable while 3.3% is unexplained. This remaining 3.3% could be caused by other factors or variables not built into the model. The high value of R-square is an indication of a good relationship between the dependent and independent variables.

The value of the adjusted R^2 is 0.850. This shows that the regression line captures more than 85% of the total variation in profitability caused by variation in the explanatory variables specified in the equation with less than 15% accounting for the error term.

Testing the statistical significance of the overall model, the F-statistic was used. The model is said to be statistically significant at 5% level because the F-statistics computed value of 14.015 (p value = .000) is greater than the F-statistics table value of 4.76 at $df_1=3$ and $df_2=6$.

The test of autocorrelation using Durbin Watson (DW) test shows that the DW value of 2.882 falls within the inconclusive region of DW partition curve. Hence, it can clearly be concluded that there exists no degree of autocorrelation.

Table 2 shows the regression results of the effect between the dependent variable, reported profit at fair value accounting and the independent variables namely; depreciation (DEP), taxes (TAX) and dividend (DIV). The regression results showed that the estimated coefficients of the regression parameters have negative signs and thus conform to our economic a-priori expectation.

The implication of these signs is that the dependent variable, reported profit is negatively influenced by depreciation (DEP), taxes (TAX) and dividend (DIV). This means that an increase in the independent variables will bring about a decrease in the dependent variable, reported profit.

The coefficient of determination, R-square of 0.927 implied that 92.7% of the sample variation in the dependent variable profitability is explained or caused by the explanatory variable while 7.3% is unexplained. This remaining 7.3% could be caused by other factors or variables not built into the model. The high value of R-square is an indication of a good relationship between the dependent and independent variables.

The value of the adjusted R^2 is 0.891. This shows that the regression line captures more than 89.1% of the total variation in profitability caused by variation in the explanatory variables specified in the equation with less than 10.9% accounting for the error term.

Testing the statistical significance of the overall model, the F-statistic was used. The model is said to be statistically significant at 5% level because the F-statistics computed of 25.472 (p value = .000) is greater than the F-statistics table value of 4.76 at $df_1=3$ and $df_2=6$.

The test of autocorrelation using Durbin Watson (DW) test shows that the DW value of 1.125 falls within the inconclusive region of DW partition curve. Hence, it can clearly be concluded that there exists no degree of autocorrelation.

4.1 Discussion of findings

Based on the empirical analysis of the comparative financial state of the sampled companies after converting the historical cost profit account to current cost (fair value) accounts, it was clearly seen that the reported profit using current cost accounting prices was much lower than that of the historical and most of the companies operated at a loss unknowingly. The study revealed that both historical cost and fair value (current cost) accounting have significant effect on reported profit.

Additionally, using depreciation charges as one of the major variables of the study for reporting profit, it was discovered that historical cost accounting made a lower depreciation to be charged against the revenue. This

145

result is in line with the work of Gay (1993); Mathews and Pevera (1996) whose analyses showed that the depreciation charged to the revenue using historical cost were low as compare to current cost method thereby making reported profit to be overstated.

Finally, tax bill and dividends declared during the period are in question. Using the historical cost reported profit to meet these obligations may lead to the companies touching their capital which is a serious threat to the service of the company. This finding concored with the results of Paton (2000) and Tearney (2004) and was also corroborated by Teemu (1991) who coincidentally stated that any attempt to use historical cost method in the current period would lead to the reduction in capital.

5.0 Conclusion/Recommendations

5.1 Conclusion

Based on the findings of the study, it is concluded that the amount calculated as depreciation, charged as taxes and paid as dividends greatly influence the operating profit of the company. This simply means that the method of profit measurement will greatly influence the amount charged as taxes, depreciation and dividend on the profit of the company. Since the profit reported by the company is directly related to the operating expenses of the company and since accounting basis adopted by the company directly relates to the reported profit, it therefore follows that the amount charged as taxes, calculated as depreciation and payout as dividends directly affect the operating profit of the company. The profit measurement method directly influences the amount calculated as depreciation, determines the amount charged as taxes and stipulates the amount paid as dividend from the reported profit of a given period.

5.2 Recommendations

Based on the findings of the study, the following recommendations were made:

1. Since inflation has made historical cost method of accounting to be inadequate, transactions and accounts should be made inflation compliant to ensure that profits reported from such transactions are not misleading. The historical financial statements should be published together with current cost financial statements to lay bare before the investors and shareholders.

2. The Securities and Exchange Commission of Nigeria should make current cost statements a precondition for filing annual returns in the commission. The submission of accounts and financial statements adjusted for effects of price changes should be made one of the conditions for firms to be listed in the stock market. This action will fairly protect the interest of investors especially in periods of rapid price changes.

3. The differences in profits measured on historical and those measured on current cost methods impact the going concern of the firm differently. The historical cost method overstates the reported profit of the firm, it is hereby recommended that during the period of changing prices, the assets of the firms should be revalued to reflect the price level changes before depreciation is calculated and charged to the accounts. This will give a high depreciation charge and high depreciation charge means low profit and vice versa.

4. Accounting bodies in Nigeria should organize workshops for the accountants and managers of companies to create enough awareness on current cost accounting and the need to depart from the historical cost accounting method during inflationary period.

5. Companies should prepare their financial report using both historical cost and fair value (current cost) methods simultaneously. This will allow the companies to know the true financial position of their companies before declaring dividend and other benefits.

REFERENCES

American Accounting Association (1986). Report of the committee on human resources; *The Accounting Review Supplement.* XLVIII, 115-123.

Anao, A. R. (1987). *A blue print for Inflation Accounting in Nigeria*. Benin: University of Benin Press.

Anao, A. R. (1989): An introduction and limitation of current cost accounting for decision making. *The Nigerian Accountant,* 11(1), 14-23.

Ajayi, C. E. (1987). Mandatory fair value accounting and information asymmetry: evidence from the European real e state industry. *Manage-   ment Science* forthcoming.

Balsely, H. C. & Clover, V. T. (1988). *Research for business decisions: Business research method* (4th ed.). Ohio: Horizons Publishers.

Barry, A. J. (1980). *Supplement on statement of standard accounting practice*. (SSAP 16). Current Cost Accounting. London: HFL Publishers.

Beredugo, S. B. (2007). The effect of Inflation on reported profits. An unpublished project.

Blake, W. R. (1959). Audit fees: A meta-analysis of the effect of supply and demand attributes. *Contemporary Accounting Research,*   23 (1), 141-191.

Edward, E. O. (1995). The state of current value accounting. *The Accounting review*, 74(2), 220-222.

Edward, E. O. & Bell, P.W. (1991). *The theory on   measurement of business income*. Los Angeles. University of California Press.

Farmer, E. R. (1985). Accounting for the effects of changing prices. Acceptable compromise or controversial rejected? *London Association of Chartered Certified Accountants Student's News letter,* 6, 2-4.

Financial Accounting Standards Board (1980). Qualitative characteristics of accounting information. *Statement of financial accounting concepts No. 2.*

Financial Accounting Standards Board (2006). Fair value measurements. *Statement of Financial Accounting Standards No. 157*.

Friedman, A. I. (1986). An investigation of revaluations of   tangible longlived assets. *Journal of Accounting Research,* 31 (3), 1-38.

Gay, R. (1993). *Positive accounting theory*. Englewood Cliffs, NJ:Prentice-Hall.

Glautier, H. & Underdown, P. (1986). *Management and cost accounting principles.* East Sussex, Cassel Limited.

Gore, E. D. & Herz, R. T. (2010). *Fair value accounting and the conceptual frame work*. ASBBS Annual Conference: Las vehas.

Grant, T. (2008). Perspective: Fair value accounting: public policy and external affairs. Retrieved October 4, 2010, from www.grantornton.com.

Hendriksen, E. S. (1982). Accounting theory. Illinois: Richard D. Irwin.

Igben, R. O. (2004). Financial accounting made simple: ROI Publishers 2004.

Jenning, A. R. (1986). *Financial accounting manual* (3rd Ed). London: DP Publication.

King, A. M. (2006). *Fair value for financial reporting: Meeting the FASB Requirement*. John Wiley & Sons. Hoboken, N.J.

Lewis, J., & Pencil. W. (1988). An experiment in fair value accounting: UK investment   vehicles.   *European Accounting Review,* 17 (2), 271-303.

Mathew, M. R. & Perera, M. H. (1996). *Accounting theory and development.* Austria International Thompson Publishing.

Meigs, J. (1984). *Accounting the basis for business decision.* New York: MacGram Hall.

Meigs, J. & Hendriken, M. K. (1982). Resource allocation   decisions in audit engagements.   *Contemporary Accounting Research,* 14 (3), 481-500.

Millichamps, A. H. (1989). *Foundation accounting: An instructional manual* (3rd Ed). London: DP Publication.

Ogolo, M. B. (1996). *Student guide to writing research and project proposals*. Port Harcourt: City Circle Press.

Ogundele, O. A. (1981). Background survey to current controvers inflation and accounting information. *The Nigerian Accountant,* 14(3), 16-28.

Paton, W. A. (2000). *An introduction to corporate accounting standard*. (6th Edition) London: Pitman.

Pizzey, A. (1980). *Accounting and finance. A firm foundation*. London. Cambridge University Press.

Richard, L. & David P. (1996). *Advanced financial   accounting*; 5th edition; London: Holmes.

Simon, J. R. (1987). The effect of audit firm size on audit prices: A study of the Australian Market. *Journal of Accounting and Economics,* 6 (2), 133-151.

Slimmings, S. (1994). *Management forecasts and litigation   risk.* Working paper, University of British Columbia.

Solomon, S. (1997). The conservatism principle and the symmetric timeliness of earnings. *Journal of Accounting and Economics,*   24 (1), 3-37.

Tearney, B. W. (2004). Continuing the normative dialog. illuminating be asset – liability theory. *Accounting Horizons.*

Teemu, A. I. (1991). Adequacy of depreciation allowance under inflation. *Journal of Business Economic,* 15(10), 43.

Turner, D. H. (2000). *Costing.* 2nd Edition. London: DP Publication.

Weirs, W. N. (2005). *Accounting theory:* A conceptual and practical guide. Port Harcourt: Alheri Integrated Service.

Williams, E. A (1977). Fair value disclosures by bank holding companies. *Journal of Accounting and Economics,* 22 (1-3), 79-117.

Table 1: Regression results of the effect of historical cost accounting on reported profit

DEPENDENT VARIABLE: Reported Profit (RPHC)

VARIABLE	ESTIMATED COEFFICENTS	STANDARD ERROR	T-Statistic	P- Value
Constant	1511.098	359.016	4.209	.000
DEP	-.003	.001	-3.023	.001
TAX	2.580	.911	2.832	.002
DIV	.265	.079	3.363	.000

R = .982
R-Square = .967
Adjusted R-Square = .850
SEE = 137343.8390
F – Statistic (df$_1$=3 & df$_2$=6) = 14.015 (p 0.000)
Durbin Watson Statistic = 2.882

Source: Researcher's estimation, 2011

TABLE 2: Regression results of the effect of current cost (fair value) accounting on reported profit

DEPENDENT VARIABLE: Reported Profit (RPFV)

VARIABLE	ESTIMATED COEFFICENTS	STANDARD ERROR	T-Statistic	P- Value
Constant	967.137	259.634	3.725	.000
DEP	-.395	.140	-2.824	.002
TAX	.180	.061	2.946	.001
DIV	.956	.280	3.415	.000

R = .963
R-Square = .927
Adjusted R-Square = .891
SEE = 58295.00675
F – Statistic (df$_1$=3 & df$_2$=6) = 25.472 (p 0.001)
Durbin Watson Statistic = 1.125

Source: Researcher's estimation, 2011