Nigeria’s Financial Reporting Council issues new regulations for the inspection and monitoring of reporting entities

Executive summary

The Financial Reporting Council of Nigeria (FRC), in exercise of its powers under sections 23(e) and 73 of the Financial Reporting Council of Nigeria Act, No. 6, 2011 recently issued regulations for the inspection and monitoring of reporting entities to ensure compliance with Nigerian financial reporting standards and the relevant code of corporate governance (the Regulations). The Regulations have an effective date of 6 October 2014.

The Regulations contain detailed steps, requirements and processes for the monitoring and inspection of an entity’s financial reports. They introduce grounds for enforcement, sanctions, penalties, appeal, and upon whom the guidelines will be applicable.

The legal basis for the Regulations may however be open to challenge as it would appear that the powers conferred on the relevant Minister for Trade and Industry to make regulations under section 73 of the FRC Act 2011 are in respect of the administration of the FRC Act.

The new Regulations do not only provide for such administrative guidance, but also prescribe new offenses and penalties and introduce charges and levies payable by entities for consultation with the council on any issues for clarification on the application of the FRC Act.
Detailed discussion

**Scope of the Regulations vis-à-vis the FRC Act**

Section 2 of the Regulations suggests that the FRC Act applies to all entities that apply any financial reporting standards in the preparation and presentation of its financial statements or other financial documentation. This is at variance with the FRC Act which restricts the regulatory powers of the FRC to public interest entities i.e., quoted and unquoted companies and organizations required by law to file returns with regulatory authorities but excluding private companies that routinely file returns to the tax authorities and the Corporate Affairs Commission.

It also contradicts the recent judgment of the Federal High Court in Eko Hotels Limited (EHL) V. the Financial Reporting Council of Nigeria on the powers of the FRC in relation to the regulation of private companies.

The Court had ruled that the FRC is empowered to regulate public interest entities; public companies, professional accountants and other professionals engaged in the preparation and presentation of financial statements but should not extend powers to private companies with reporting requirements to only the Federal Inland Revenue Service (FIRS) and the Corporate Affairs Commission (CAC).

As the FRC has filed an appeal against this judgment, there is a likelihood that entities may seek to challenge the application of these provisions as section 73 of the Act relied upon in making the Regulations, does not expressly grant the FRC the power to expand the scope of the principal Act, impose levies and create penalties for non-compliance.

**Offenses and penalties**

The new Regulations provide for penalties and offenses following the discovery of material errors whether or not they lead to the restatement of financial statements. The penalties may be imposed on the defaulting entity, the external auditor or audit firm and other relevant professionals. The penalty is based on the category of non-compliance.

Penalties for non-compliance that should not lead to a withdrawal or restatement of financial statements are categorized into types 1-5 with monetary consequences ranging from N5 million to N100 million. The type 6 error or non-compliance would require a withdrawal of the financial statements and result in a penalty of N500 million to N5 billion for each year requiring such restatement. The specific amount imposed would depend on the market capitalization of the defaulting entity.

Payment for any penalty imposed must be made within 14 days of receipt of the penalty notice otherwise an additional penalty of 0.1% of the imposed penalty will accrue for each day of default.

These penalties are a significant increase to the penalties initially provided for in the FRC Act. The FRC Act sets out two main penalties for public interest entities. The first is a penalty of N10 million or two-year jail term or both for failure to file financial reports with the FRC. The second is a penalty of N20 million for an entity's failure to comply with the FRC's notice to re-state its financial statement.

**Consultation fee**

The Regulation states that the time spent in discovering errors on non-compliance will be charged to the entity by way of management time at N250,000 only per hour. An on-site inspection fee of N1 million per day will also be paid by an entity whenever the council members inspect an entity's records in order to confirm a case of non-compliance.

FRC may grant an appointment to an entity or its auditors to give clarification on financial reporting elements. A non-refundable fee of N100,000 is payable for each appointment and a management time charge of N500,000 per hour thereafter for each meeting. These fees and charges in the Regulations
appear exorbitant considering that the FRC is set up to assist in ensuring compliance with financial reporting standards. Charges that could significantly increase the financial burden of entities may dissuade entities from seeking clarity from the FRC on gray areas with respect to the financial treatment of certain transactions.

Implications
Given the substantial penalties imposed by these Regulations, it is expedient that in spite of the uncertainty around the basis and scope of the Regulations, affected entities should ensure strict compliance with relevant accounting and auditing standards in the preparation and presentation of the records in order to avoid any investigation by the FRC.

Appeal procedure
The Regulations introduce a fee for appeals to be heard by the Technical and Oversight Committee (TOC) of the FRC within 14 days and the payment of a non-refundable application fee of N1 million. This appeal procedure is contained in the FRC Act but no application fee is required of the applicant.

For additional information with respect to this Alert, please contact the following:

Ernst & Young Nigeria, Lagos
▶ Abass Adeniji +234 802 301 3597 abass.adeniji@ng.ey.com
▶ Edem Andah +234 708 768 1113 edem.andah@ng.ey.com
▶ Chinyere Ike +234 803 571 7211 chinyere.ike@ng.ey.com
▶ Ogochukwu Isiadinso +234 802 712 5450 ogochukwu.isiadinso@ng.ey.com
▶ Peace Izedonmi +234 146 304 7980 peace.izedonmi@ng.ey.com

Ernst & Young Advisory Services (Pty) Ltd., Johannesburg
▶ Justin Liebenberg +27 11 772 3907 justin.liebenberg@za.ey.com

Ernst & Young LLP (United Kingdom), Pan African Tax Desk, London
▶ Leon Steenkamp +44 20 7951 1976 lsteenkamp@uk.ey.com
▶ Gonçalo Dorotea Cevada +44 20 7951 2162 gcevada@uk.ey.com

Ernst & Young LLP, Pan African Tax Desk, New York
▶ Dele A. Olaogun +1 212 773 2546 dele.olaogun@ey.com
▶ Mzukisi Ndzipo +1 212 773 9917 mzukisi.ndzipo@ey.com
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