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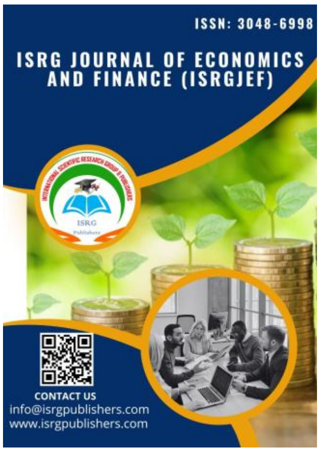

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EXECUTIVE COMPENSATION AND FINANCIAL REPORTING QUALITY IN THE AGRICULTURE SECTOR

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Abstract

This study examined the effect of executive compensation on the financial reporting quality of agricultural companies listed on the Nigerian Exchange Group (NGX), with firm size serving as a control variable. The research utilized panel least squares regression and was based on secondary data collected from five agricultural firms between 2019 and 2023. Discretionary accruals were used to proxy financial reporting quality, while executive compensation and the interaction between firm size and compensation were the key explanatory variables. Regression results showed that executive compensation had a statistically significant positive effect on financial reporting quality ($\beta = 22.83$, $p = 0.0106$), suggesting that higher compensation is associated with reduced earnings manipulation. Conversely, the interaction between firm size and executive compensation was negatively significant ($\beta = -2.62$, $p = 0.0090$), indicating that the positive influence of executive compensation on reporting quality diminishes as firm size increases. In conclusion, the study found that effective executive compensation structures enhance financial reporting quality, particularly in smaller agricultural firms. These findings have important implications for corporate governance practices, encouraging policy reforms that align executive incentives with transparency and accountability in financial reporting.

Key Words: Executive Compensation, Financial Reporting Quality, Corporate Governance

1. INTRODUCTION

In the ever-changing world of corporate governance and financial integrity, stakeholders all over the world are very concerned about the quality of financial reporting. Financial statements are important ways for businesses to tell investors, regulators, and the public about their performance, financial situation, and how they are managing their resources. If this kind of information is changed, either on purpose or by accident, it can hurt investor confidence and have big effects on the economy (Chkir et al., 2024). The reliability of financial reporting is closely linked to the actions and motivations of managers. Executive pay is one of many factors that influence these decisions, and it has gained more attention in academia. Regulators are meant to ensure that management and shareholders have the same goals. But incentives that aren't right or too high might also lead to opportunistic behaviour, such as manipulating earnings or using aggressive accounting methods (Jensen & Meckling, 1976).

Executives, particularly those in important financial and strategic positions, shape financial reports. Executives, particularly those in important financial and strategic positions, design their pay packages with wages, incentives, stock options, and other benefits to motivate them to perform optimally (Owota, 2022). Still, there are questions regarding whether these kinds of payment systems really encourage openness or, on the other hand, provide managers with reasons to manipulate things to fulfil performance goals and make more money for themselves (Healy & Wahlen, 1999). The agricultural sector is crucial in many economies since it helps with food security, job creation, and economic diversity. The industry is a big part of Nigeria's non-oil GDP and helps people in rural areas make a living. Agricultural companies generally have trouble with governance and financial reporting because of things like informal operating structures, changing production cycles, and not enough regulatory control (Nwankwo et al., 2020). These traits make the industry especially susceptible to knowledge asymmetry and poor financial reporting. As the requirement for accurate and high-quality financial reporting grows, we need to pay greater attention to the governance systems that affect these outcomes in agricultural companies. Executive pay is one of these mechanisms. Depending on how it is set up, it may either help or hurt the integrity of reporting. Studies have indicated that there is no clear link between executive compensation and reporting quality. The evidence suggests that the nature of this link may depend on the circumstances, such as the industry and the regulatory environment (Bebchuk & Fried, 2004).

Also, when examining the link between CEO pay and reporting quality, don't forget company-specific factors like size. Leaders may find it more difficult to alter results in larger companies due to increased scrutiny and internal controls. But they could also have more complex operations, giving them more freedom in financial reporting (Roychowdhury, 2006). So, it's important to understand how company size affects control to give more detailed information on how executive incentives impact reporting behaviour. In Nigeria, most research on CEO pay and its effects has been done in the banking and industrial sectors, where corporate governance reforms are more established (Owota et al. 2022). However, the agriculture industry, which is experiencing increased investment and formalisation, has received less attention. The capital structures, ownership patterns, and governance methods of agricultural companies are so different that they need their study of financial reporting practices (Okonkwo & Uche, 2018). It is important for investors, public policy, credit allocation, and sustainable development to have trustworthy financial reporting in the agriculture sector. Poor financial reports can make it harder to obtain loans, make investors less likely to invest in the country, and hurt growth in certain sectors. Because of this, it is very important to understand what makes financial reporting excellent in Nigeria's agricultural companies. Therefore, this study wants to look at how CEO pay affects the accuracy of financial reports for agricultural enterprises in Nigeria.

2. PROBLEM STATEMENT

The credibility of financial reporting has become a major issue in the worldwide discussion over corporate governance and investor protection in the last several decades. Stakeholders need high-quality financial reports to make smart economic choices, use resources wisely, and judge how well managers are doing their jobs. But worries about profit profitmanipulation, creative accounting, and lack of openness have made many wonder what motivates and governs executives (Dechow, Ge & Schrand, 2010). Executive pay is one of the most problematic governance methods related to the quality of financial reporting. Compensation packages are meant to match the interests of executives with those of shareholders, but they can sometimes unintentionally encourage executives to manipulate results, especially when they are linked to financial performance criteria (Healy & Wahlen, 1999). This paradox has led to academic discussions and government action, as too much or badly structured pay has been linked to financial scandals and business failures throughout the world (Bebchuk & Fried, 2004).

These problems are also present in Nigerian businesses. Despite significant improvements in corporate governance, the issue of financial misreporting persists. Most of the research on CEO pay and the quality of financial reporting in Nigeria has been done in the banking, oil and gas, and industrial sectors. These are the areas where governance frameworks are stronger and regulatory scrutiny is higher (Okonkwo & Uche, 2018). However, the agriculture sector is still not getting enough attention, even though it is becoming more important to the economy and more formalised. Climate change, seasonal output, and changing commodity prices are just some of the things that make it challenging for agricultural entrepreneurs in Nigeria to run their businesses. These traits may lead CEOs to smooth out results or provide unduly positive financial reports to fulfil expectations, get funding, or justify pay (Nwankwo, Umeh, & Adebayo, 2020). If these reporting errors aren't closely examined, they could harm stakeholder trust and make it harder to get financing, both of which are vital for the sector's growth.

Furthermore, there isn't much real-world information on how things like size affect executive pay and how that affects the quality of financial reporting in agricultural companies. Depending on how well the company's internal controls, board, and outside monitoring work, the size of the company may make it easier or harder to manipulate results (Roychowdhury, 2006). If you don't understand this moderating factor, policy suggestions to improve industry reporting may not work or be aimed at the right people. The lack of studies focussing on individual sectors is a significant problem in the literature, making it more difficult to develop effective governance strategies for businesses. Some studies indicate that executive incentives lead to better reporting when there is robust monitoring, but others show the reverse when there are inadequate accountability mechanisms (Jensen & Meckling, 1976). This mismatch makes it even more clear that we need to do more study in context, especially in fields like agriculture that are

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important to national growth but aren't researched as much. Because these problems have not been rectified, this study was started to look at how CEO pay affects the quality of financial reporting by Nigerian agricultural companies. The study also aims to determine whether the size of a company significantly impacts this relationship.

Hypotheses

$H_0$1: Executive compensation has no significant effect on the financial reporting quality of agricultural companies in Nigeria.

$H_0$2: Firm size does not significantly control the relationship between executive compensation and financial reporting quality of agricultural companies in Nigeria.

3. LITERATURE REVIEW

Financial Reporting Quality

Quality of financial reporting means how well financial statements provide stakeholders clear, accurate, and useful information that helps them make smart economic choices. It demonstrates the extent to which a firm's financial records accurately reflect the company's economic performance and overall health (Dechow, Ge & Schrand, 2010). High-quality financial reports reduce the difference in information between business management and outside users like investors, regulators, and analysts. This builds trust in the financial system. This concept is crucial for corporate governance and accountability because it informs stakeholders about a company's financial performance and operational effectiveness. High-quality financial reports enhance a company's credibility, boost investor confidence, and facilitate more efficient use of funds (Francis et al., 2008). On the other hand, inadequate reporting can confuse users, hide inadequate performance, and lead to incorrect decisions, which can have serious effects on investors and the economy as a whole.

Financial reporting quality has to do with how accurate and beneficial financial information is. This includes how clear, consistent, and full the reports are, as well as how well they show what the company is actually doing with its money without changing the facts (Penman & Zhang, 2002). The International Financial Reporting Standards (IFRS) and other accounting standards establish rules to help make things consistent, but people still have to use their judgement when applying these standards. This subjectivity can allow managers more freedom, which might make the information better or worse. Effective financial reporting depends on more than just following the rules. It also depends on companies acting ethically and having effective internal governance systems. When their pay or job security is related to how well the company does financially, managers often have reasons to change earnings or smooth out income to suit market expectations (Healy & Wahlen, 1999). Even with strict adherence to accounting rules, the quality of financial reporting can deteriorate in certain situations. Therefore, the honesty and independence of the people who make and examine financial accounts are quite important.

The rules, institutions, and industries that apply to financial reporting also impact its quality. In developing economies like Nigeria, things like insufficient implementation of accounting rules, low audit quality, and inadequate corporate governance procedures can make financial reporting less accurate (Oyerinde, 2011). This is especially worrisome in industries like agriculture, where companies have to contend with unstable markets and not much outside inspection, which makes it more likely that financial statements would be biased or incorrect.

Executives Compensation

Executive compensation is the total amount of money and other benefits that top-level managers, like chief executive officers (CEOs), chief financial officers (CFOs), and executive directors, receive for overseeing and managing an organisation's operations. This pay is meant to help companies identify, keep, and encourage competent people who have the skills and strategic vision to help them reach their goals (Jensen & Murphy, 1990). Executive pay has become a crucial topic in discussions about business management, particularly as companies strive to align managers' interests with those of shareholders. The parts that make up CEO pay are usually more complicated and bigger than those that make up basic employee pay. These include a base pay, bonuses, stock options, long-term incentive schemes, pension contributions, and other perks. These parts are typically dependent on performance and are set up such that the executive's awards are tied to the company's financial success (Core, Holthausen & Larcker, 1999). The main idea is that when executives are paid based on company performance, they are more likely to make decisions that increase stock value.

However, the way CEO pay is structured and how open it is have gotten a lot of attention from both academics and the public because of worries about too much pay, poor supervision, and possible conflicts of interest. Executives can sometimes influence their pay, which may not be in the best interests of the firm or its stakeholders (Bebchuk & Fried, 2004). This is especially true when governance systems are inadequate. This worry is especially important in emerging economies, where there may not be as much regulatory supervision or shareholder activity. In principle, well-designed executive pay packages may make a company work better by lowering agency issues, which are conflicts that happen when managers put their interests ahead of those of shareholders (Eisenhardt, 1989). According to agency theory, companies can reduce opportunistic behaviour by linking executive compensation with performance measurements. This makes managers' aims more in line with owners' goals. However, the effectiveness of this alignment heavily depends on the methods used to assess and monitor performance. Institutional, cultural, and economic variables also affect the idea of executive pay. In emerging economies like Nigeria, CEO pay arrangements are frequently less clear and less standard, which raises problems about justice, accountability, and value creation (Ogbechie & Koufopoulos, 2020). The relationship between pay and performance may be tougher to determine in fields like agriculture, where financial risks and returns can change quickly. This makes it harder to understand how CEO pay might encourage responsible management and accurate financial reporting.

Stewardship Theory

Stewardship theory is a way of running an organisation that says managers, or stewards, should behave in the best interests of the organisation and its stakeholders instead of looking out for their interests. This view is different from agency theory, which says that managers are naturally opportunistic and need to be actively watched and rewarded to ensure that they act in the best interests of shareholders (Davis, Schoorman & Donaldson, 1997). According to stewardship theory, managers are happier when their organisations do well, and they are devoted to their tasks and responsibilities because they are motivated by trust and loyalty. The main idea behind stewardship theory is that CEOs are honest and can make sure their aims are in line with those of the company without the need for many outside controls or complicated incentive systems. The hypothesis is based on the idea that stewards live in a collectivist society, where they value working together, doing well over the long term, and keeping the organisation stable (Donaldson & Davis, 1991). Therefore, even if there aren't any contractual responsibilities, stewards should make judgements that increase the value of the company, keep things open, and encourage long-term growth.

Stewardship theory says that in the context of corporate governance and CEO pay, both financial and non-financial rewards should encourage a feeling of responsibility and dedication to the organisation's objective. Agency theory says that performance-based compensation can help keep people from acting in their own best interest. Stewardship theory, on the other hand, says that leaders don't need big incentives to do what's best for the company. Instead, governance frameworks should grant managers more power, encourage people to be involved in decision-making, and put more emphasis on trust than on control (Letza, Sun & Kirkbride, 2004). Stewardship theory is especially useful in businesses that emphasise long-term partnerships, a strong organisational culture, and strong moral principles. In these kinds of situations, trust between the board and CEOs may lead to new ideas, more responsibility, and better financial reporting. Managers are more inclined to ensure that financial disclosures are clear and correct when they regard themselves as stewards. They believe that such responsibility is part of their obligation to the company and its stakeholders (Davis et al., 1997). In the agency model, such actions could only occur due to fear of punishment or the promise of money.

Prior Studies

Recent research has looked at the link between CEO pay and company performance in great detail, focusing on both financial results and how well the company is run. For example, Raithatha and Komera (2016) looked at Indian companies and discovered that CEO pay is linked to the size of the company and how well it has done in the past. This finding suggests that the pay structure is based on performance. Aluko et al. (2020) also looked at Nigerian listed businesses and found a substantial positive link between CEO remuneration and company performance. This evidence suggests that incentive alignment works well in developing markets. These results back up what Qiao and Wang (2017) found earlier: that greater pay for executives in Chinese state-owned businesses is linked to better financial performance. In general, these studies show that well-structured pay packages can motivate executives to work more to achieve better outcomes for the company.

Another important area of research looks at how CEO pay affects how willing companies are to take risks. Bouteska, Sharif, and Abedin (2024) looked at U.S. non-financial companies and found that giving leaders many stock options makes them more likely to take risks, especially when they think such risks would pay off in the long run. Kweh et al. (2022) also found that when companies don't have enough money, the link between CEO pay and performance weakens, which might lower the incentives to take risks. These results indicate that the way executives are paid, specifically the use of long-term equity incentives, is very important in determining how they make decisions that influence the company's risk profile and long-term viability.

Some researchers have examined the unexpected effects of certain pay systems, particularly their potential to lead to earnings management. Lyu and Zhang (2017) looked at Chinese manufacturing companies and found that there was a positive correlation between pay and earnings manipulation. They said that short-term remuneration makes CEOs more likely to change financial statements to achieve performance goals. This finding aligns with other research indicating that poorly constructed pay schemes may encourage unethical accounting methods to protect or enhance executive bonuses. These ideas are crucial for understanding why CEO contracts need to include a balance between short-term and long-term rewards.

The management style and board dynamics significantly influence executive compensation. Al-Najjar (2017) said that UK travel and leisure companies with excellent governance frameworks tend to compensate their CEOs more based on how well they do their jobs. Agyemang-Mintah (2019) stressed how important it is for UK financial businesses to have effective compensation committees that guarantee that CEO pay is in line with the company's goals. Agrawal and Nasser (2019) also found that having blockholders on boards helps to guarantee that pay structures are more in line with the interests of shareholders and the value of the company. These results show that governance supervision is necessary to ensure that pay policies don't lead to opportunistic behaviour.

Finally, recent studies have looked at how the traits of executives and changes in the job market affect pay. This has broadened the field of compensation study. Giannakis et al. (2024) found that U.S. S&P 500 corporations pay their executives more when they have more education and are affiliated with prominent institutions, especially when they are moving from one company to another. Akram et al. (2019) also observed that management authority has a big effect on compensation structures, which may therefore have an effect on how well a company does. In their thorough research, Edmans, Gabaix, and Jenter (2017) concluded that a nuanced understanding of CEO remuneration must consider both internal governance and external market pressures. These points of view show how challenging it is to create pay structures that inspire CEOs while also keeping them accountable and making sure they do their jobs well.

4. METHODOLOGY

The study adopted an ex post facto research design, which is appropriate for analyzing past events and existing data without manipulating any variables. The research focuses on examining the effect of executive compensation on the financial reporting quality of agricultural companies in Nigeria. The population of the study consists of the five (5) agricultural companies listed on the Nigerian Exchange Group (NGX) as of 2024. These firms were selected based on their consistent listing and availability of relevant financial data during the study period. The study utilizes secondary data obtained from the published annual reports and financial statements of the selected companies for the period 2019 to 2020. Data on executive compensation were extracted from the notes to the accounts and corporate governance sections, while proxies for financial reporting quality were derived from accrual-based metrics and financial disclosures. Descriptive and inferential statistical techniques, including multiple regression analysis, will be used to examine the relationship between the variables. The analysis will be carried out using E-Views statistical software, ensuring accuracy and reliability in testing the hypotheses of the study. The following regression model is specified:

$$FRQ = \beta_0 + \beta_1 EXCOMP + \beta_2 FSIZE + \varepsilon$$

Where:

FRQ = Financial Reporting Quality (dependent variable, proxied using discretionary accruals model)

EXCOMP = Executive Compensation (independent variable, measured by total compensation)

FSIZE = Firm Size (control variable, measured as the natural logarithm of total assets)

β_0 = Intercept

β_1, β_2 = Coefficients of the explanatory variables

ε = Error term

5. RESULT, IMPLICATIONS AND CONCLUSION

Descriptive Result

	DISCRE_ACCRU	EXCOMP	FSIZE
Mean	-7803488.	17167702	6.632082
Median	0.000000	1742787.	7.083356
Maximum	33883984	1.01E+08	9.084822
Minimum	-1.09E+08	0.000000	0.000000
Std. Dev.	28787510	32046428	2.627795
Skewness	-2.416044	1.659553	-1.892993
Kurtosis	8.489111	4.057241	5.413611
Jarque-Bera	55.70772	12.63981	20.99917
Probability	0.000000	0.001800	0.000028
Sum	-1.95E+08	4.29E+08	165.8020
Sum Sq. Dev.	1.99E+16	2.46E+16	165.7274
Observations	**25**	**25**	**25**

Source: Eview 9.0

The descriptive statistics for the variables in the study discretionary accruals (DISCRE_ACCRU), executive compensation (EXCOMP), and firm size (FSIZE) provide insights into the mean value of discretionary accruals is approximately -7.8, with a median of 0, indicating a tendency toward negative accruals, suggesting earnings management in downward direction. The data is highly dispersed, as shown by a large standard deviation of about 28.8. The negative skewness (-2.42) and high kurtosis (8.49) imply a left-tailed and leptokurtic distribution, deviating significantly from normality. The Jarque-Bera test (55.71, $p < 0.01$) confirms this non-normality. For executive compensation, the mean is around 17.2, but the median is significantly lower at about 1.7, reflecting a right-skewed distribution (skewness = 1.66), where a few executives receive much higher compensation. The high standard deviation (32) also indicates wide variability. Kurtosis (4.06) suggests a moderate departure from normality, which is also supported by the Jarque-Bera test (12.64, $p = 0.0018$). Firm size has a mean of 6.63 and a median of 7.08, with values ranging from 0 to 9.08, suggesting some firms are very small while others are significantly larger. The negative skewness (-1.89) and kurtosis (5.41) show the data is left-skewed and leptokurtic, with the Jarque-Bera test (20.99, $p = 0.00003$) confirming significant deviation from normality.

Regression Result

Dependent Variable: DISCRE_ACCRU

Method: Panel Least Squares

Date: 05/17/25 Time: 14:30

Sample: 2019 2023

Periods included: 5

Cross-sections included: 5

Total panel (balanced) observations: 25

Variable	Coefficient	Std. Error	t-Statistic	Prob.
EXCOMP	22.82550	8.171140	2.793430	0.0106
FSIZE*EXCOMP	-2.619373	0.914761	-2.863453	0.0090
C	-4721776.	5092721.	-0.927162	0.3639

R-squared	0.564167	Mean dependent var	-7803488.
Adjusted R-squared	0.524545	S.D. dependent var	28787510
S.E. of regression	19849913	Akaike info criterion	36.55746
Sum squared resid	8.67E+15	Schwarz criterion	36.70373

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Log likelihood	-453.9683	Hannan-Quinn criter.	36.59803
F-statistic	14.23901	Durbin-Watson stat	2.950771
Prob(F-statistic)	0.000108		

Source: Eview 9.0

The regression results show that executive compensation (EXCOMP) has a statistically significant and positive effect on discretionary accruals (DISCRE_ACCRU), as indicated by a coefficient of 22.83 and a p-value of 0.0106. This means that an increase in executive compensation is associated with an increase in discretionary accruals, suggesting a potential incentive for executives to manipulate earnings to align reported performance with personal compensation goals. However, the interaction term FSIZE*EXCOMP, which represents the control effect of firm size on the relationship, is negative and also statistically significant with a coefficient of -2.62 and a p-value of 0.0090. This suggests that as firm size increases, the influence of executive compensation on discretionary accruals decreases, indicating that larger firms may have stronger governance mechanisms that limit opportunistic earnings management.

In terms of model performance, the R-squared value of 0.5642 indicates that about 56% of the variation in discretionary accruals is explained by the independent variables. The adjusted R-squared of 0.5245 also confirms a good fit, accounting for the number of predictors. The F-statistic of 14.24 and its associated probability value of 0.0001 indicate that the model is statistically significant overall. Additionally, the Durbin-Watson statistic of 2.95 suggests minimal autocorrelation in the residuals, which supports the reliability of the model.

Test of Hypothesis

$H_0$1: Executive compensation has no significant effect on the financial reporting quality of agricultural companies in Nigeria.

The regression result shows that the coefficient of executive compensation (EXCOMP) is 22.82550 with a p-value of 0.0106, which is less than the 0.05 significance level. This indicates a statistically significant relationship between executive compensation and discretionary accruals (used as a proxy for financial reporting quality). Since the p-value is below 0.05, we reject the null hypothesis (H01) and conclude that executive compensation has a significant effect on the financial reporting quality of agricultural companies in Nigeria.

$H_0$2: Firm size does not significantly control the relationship between executive compensation and financial reporting quality of agricultural companies in Nigeria.

The interaction term (FSIZE*EXCOMP) has a coefficient of -2.619373 and a p-value of 0.0090, which is also less than the 0.05 significance level. This implies that firm size significantly moderates the relationship between executive compensation and financial reporting quality. Therefore, we reject the null hypothesis (H02) and conclude that firm size significantly controls or moderates the relationship between executive compensation and financial reporting quality in agricultural companies in Nigeria.

Implications of Findings

The findings of this study carry several theoretical, managerial, and policy implications. First, the significant positive effect of executive compensation on financial reporting quality suggests that incentive structures in the agricultural sector can influence managerial behavior regarding earnings management practices. This aligns with agency theory, which posits that aligning managers' interests with those of shareholders through appropriate compensation packages can enhance the quality of financial reporting. It implies that well-structured compensation systems may serve as effective governance mechanisms for curbing discretionary accruals and ensuring transparency in financial disclosures.

Furthermore, the moderating role of firm size indicates that the impact of executive compensation on financial reporting quality varies depending on the scale of the company. Larger firms may have more complex operations and stronger governance frameworks that enhance or limit the effects of executive incentives. This finding highlights the importance of considering firm-specific characteristics in the design and implementation of compensation policies. For policymakers and regulators, the results suggest a need to enforce tailored corporate governance standards that factor in company size, while also promoting transparency and accountability in executive remuneration schemes across the agricultural sector.

Conclusion

In conclusion, this study examined the effect of executive compensation on the financial reporting quality of agricultural companies in Nigeria, with firm size considered as a control variable. The results revealed that executive compensation significantly influences financial reporting quality, indicating that appropriate incentive structures can reduce managerial discretion and enhance transparency. Additionally, the interaction between firm size and executive compensation showed a significant negative effect, suggesting that the size of a firm moderates the relationship between executive pay and reporting practices. These findings underscore the importance of aligning executive incentives with financial integrity, while also recognizing the role organizational scale plays in shaping this dynamic.

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