JIBC

Journal of Internet Banking and Commerce

An open access Internet journal (http://www.icommercecentral.com)

Journal of Internet Banking and Commerce, August 2019, vol. 24, no. 2

CORPORATE ETHICAL STANDARD AND THE QUALITY OF SUSTAINABILITY REPORTING: EMPIRICAL EVIDENCE FROM COMMERCIAL BANKS IN NIGERIA

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Abstract

Compliance with legal requirements is mandatory for corporate entities in Nigeria, but when a decision is taken in a situation that is not legally binding, the appropriate moral decision depends on the ethical standard of the company. Sustainability reporting in Nigeria is voluntary, therefore the quantity and quality of disclosure is at the discretion of company leadership. This study evaluated the ethical behavior of Nigerian commercial banks and how it affects their sustainability disclosure quantity and quality. Focus was on the proportion of each bank's corporate annual reports that contains environmental disclosures, social responsibility disclosures and governance disclosures. Information on the banks' websites that relate to sustainability policies or activities was also considered. This work includes an extensive review of relevant literature, hinging the study on legitimacy theory. Cross-sectional research design was utilized in undertaking the study. Samples of fourteen (14) commercial banks were selected from the companies listed on the Nigerian stock exchange and studied for a period of 2008-2017 financial years. Multivariate Linear model analysis was used to test the hypothesis. Findings revealed a positive relationship between corporate ethical standard and sustainability disclosure of Nigerian commercial banks. It is hereby, recommended that company directors and stakeholders should build strong corporate ethical culture since it directly affects their sustainability, while quality sustainability reporting practice is beneficial to the reporting entity, environment and society.

Keywords: **Sustainability Information; Ethical Behavior; Corporate Report; Bank Website**

INTRODUCTION

The ethical standard of a company evaluates their actions in terms of what is morally right or acceptable, beyond legal requirements. It is good to comply with legal requirements, as expected, but when a decision is taken in a situation that is not legally binding, the appropriate moral decision is commendable and has a positive effect on reputation. A reputable company is expected to take responsible decisions and ensure their corporate representations uphold the law. Company policies and protocols should reflect the required laws binding on them and the standard of their ethical behavior [1]. Laws differ from one country to another and more stringent in some. Companies in developing countries tend to take advantage of laxities in their regulation [2]. The International Financial Reporting Standards (IFRS) state the standard requirements for a financial report. IFRS is the required reporting standard in Nigeria, issued by the International Accounting Standard Board (IASB) and enforced by the Financial Reporting Council of Nigeria (FRC). Also, in Nigeria the Companies and Allied Matters Act (CAMA), Securities and Exchange Commission (SEC) have financial reporting requirements for companies and the Central Bank of Nigeria has financial reporting requirements for banks in Nigeria.

The role of corporate reports in making investment decisions has necessitated the keen interest of investors in the reporting process. Investors have an increasing demand for more transparency and accountability. More stakeholders are now interested in a broader scope of analysis and reports for their decision making. Broader scope that includes non-financial contents such as environmental, social and governance reports [3]. Corporate reports state the results of operations in the stated reporting period, also sustainability reports are expected to present the environmental preservation activities, social responsibility projects and corporate governance compliance of the reporting entity. This practice attracts additional costs on the business. This leads to the question of ‘reason’ in a system of voluntary sustainability disclosure practice. Why would a company engage in sustainability practice and reporting?

RESEARCH OBJECTIVES

The aim of this work is to empirically examine the relationship between corporate ethical standard and sustainability disclosures of commercial banks in Nigeria. The specific objectives are to:

- Determine the relationship that exists between corporate ethical standard and the quality of sustainability disclosures published by commercial banks in Nigeria.
- Investigate whether corporate ethical standard impacts the quality of sustainability disclosures published by commercial banks in Nigeria.

LITERATURE REVIEW

Corporate ethics is the application of moral principles to the conduct of business and in the governance of personnel behavior at work. The purpose of ethics is to provide the tools for dealing with moral complexity in business. The ethical implications of business decisions must be considered before choosing a course of action [4]. Sustainability reporting guidelines that pertain to ethics and integrity are contained in the fourth edition of the global reporting initiative guidelines. These standard disclosures provide an overview of the organization’s values, principles, standards and norms, its internal and external mechanisms for seeking advice on ethical and lawful behavior, its internal and external mechanisms for reporting concerns about unethical or unlawful behavior and matters of integrity. Section 56 of the fourth edition global reporting initiative guidelines describes the organization’s values, principles, standards and norms of behavior such as codes of conduct and codes of ethics. Section 57 refers to the internal and external mechanisms for seeking advice on ethical and lawful behaviour, and matters related to organizational integrity, such as helplines or advice lines. Section 58 relates to the internal and external mechanisms for reporting concerns about unethical or unlawful behavior, and matters related to organizational integrity, such as escalation through line management, whistleblowing mechanisms or hotlines [5]. For this study, stated code of conduct, occurrence or frequency of corporate fines and dues arising from violations, tax compliance and litigations against the company or its staff on duty would be considered as a measure of ethical standard.

Activities of firms have been seen to have some adverse effect on the environment and society. The attention of managers has been called to this and the way they respond to the situation has to be reported to the stakeholders. Corporate reporting advancement occurs as society evolves and the expectations of stakeholders rise. Sustainability reporting is the practice of measuring, disclosing, and being accountable to internal and external stakeholders for organizational performance towards the goal of sustainable development [6].

There are Nigerian empirical studies on environmental and social responsibility reporting, most of which focused on Oil and gas, manufacturing or financial sectors [7-10]. Researchers justified their choice of these sectors. Studies that focused on oil and gas or manufacturing sectors explained that these sectors have more adverse effects on the environment than other sectors. Other studies that gathered data and based their findings on the financial sector noted that the Central Bank of Nigeria (CBN) has more strict regulations as regards corporate governance for Nigerian banks.

The Nigerian banking sector is sensitive to the economic and financial wellbeing of the country, therefore the operations of the sector is carefully regulated [11]. The Central Bank of Nigeria states mandatory policies for corporate governance required of banks in Nigeria, which includes some policies on social and environmental reporting. Even with this there are aspects of sustainability not included in the policy, which remain voluntary [12]. Companies in Nigeria that publish comprehensive sustainability reports are mostly multinationals that have international market standards to uphold and companies in the oil and gas industry that are considered to have major impacts on the environment [13]. Many of the Nigerian quoted companies only have short social responsibility reports or sustainability activities mentioned in the directors' report. This study considers the environmental, social and governance disclosures of the sampled data, to appropriately capture the level of sustainability reporting in each commercial bank.

Some benefits of sustainability reporting have been identified to include financial performance, gaining legitimacy and recently there have been discussions about building trust and earning reputation through sustainability reporting practice

[14]. Public relations experts agree that a way to override criticisms is by broadcasting success stories, through the media or through published corporate reports. Publishing stories in the media could be in favour or against the reputation of the company depending on who is reporting. On the other hand, it is easier for companies who practice voluntary sustainability disclosure to report when their sustainability performance is high and not when the performance is low. Relevance of corporate reporting can only be justified when information derived from the report influences the economic decisions of stakeholders and users of the report [15].

Legitimacy Theory

Legitimacy theory extends social contracting theory and involves companies responding to demands of divergent interest groups by legitimizing their actions. Legitimacy theory is defined as a generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs and definitions [16]. Legitimacy exists at the organizational level when there is congruence between organization and society value system. It is about an organization fulfilling their social contract with the society [17]. This theory is based on the notion that companies have an implied approval from society to allow them to operate, in return for performing actions beneficial to the society. It further suggests that company disclosures may be a reaction to how different stakeholder groups view the company [18]. Communication of sustainability can be considered as a means of obtaining legitimacy from stakeholders [19].

Haniffa and Cooke identified legitimacy theory as more appropriate when considering voluntary rather than mandatory social disclosure. Under legitimacy tenets the nature of industry type potentially affects sustainability disclosure, the impact of industry type on disclosure may depend on how critical the company feels their economic activities impact on society [20]. O’Donovan also noted that market-based theories are rejected as the primary explanation for environmental disclosures [21]. These theories are based on an agency theory perspective and also encompass the idea that the only important stakeholders are those who have direct financial interest in the company. Legitimacy theory has been embraced by many social and sustainability accounting and reporting researchers. Within accounting literature, it has been concerned largely with the reactive nature of organizational disclosure [22]. The theory predicts that firms disclose their sustainability activities to legitimize their operations [23].

The basic concept of legitimacy is that one group has power and authority over another. The group which has the power and authority requires approval from the group over which power is exercised in order for the relationship to exist. Legitimacy theory suggests that management can impact the perceptions which the general public has of the firm [21]. Studies have found a relationship between different measures of social responsibility reporting and major pollution accidents or environmental prosecutions which are proxies for legitimacy threats [24]. Deephouse and Carter opined that legitimacy is assessed based on expectations of social systems, values and regulations [25].

Variables and Gathering of Data

Secondary data were gathered to measure corporate ethical standard (ETS), data was gathered on clearly stated policies, fulfilment of Tax obligation, compliance with required reporting standards, any contingent liabilities arising from legal default or litigation against the firm, malpractice and scandal, scoring -1 where the company defaults or +1 where the company has not defaulted. Secondary data were also gathered to measure corporate Environmental, Social and Governance (ESG) disclosures by content analysis of integrated corporate annual reports and stand–alone sustainability reports published on the websites of the selected commercial banks. Disclosure quality was measured by classifying texts into categories on pre-selected criteria of qualitative disclosure as applied by Toms, et al. [3]. Quality scores are awarded on each report using a 0–5 qualitative scale as follows: no disclosure: 0, general rhetoric: 1, specific endeavour, policy only: 2, specific endeavour, policy specified: 3, implementation and monitoring but qualified result not published: 4, implementation and monitoring and qualified result published: 5. Data on disclosure quantity was gathered by sentence count to determine disclosure volume. Then to estimate the percentage of report devoted to sustainability disclosure, the total number of sustainability sentences was divided by total number of sentences in corporate report.

The control variables are power of shareholders, company size and Financial performance. Power of shareholders was measured by taking share capital as a percentage of net worth. Company size was measured by gross income or interest income; this captures the size of the bank's operations. Financial performance was captured by computing the return on equity. Return on equity is a profitability ratio that measures the ability of a firm to generate profits from the shareholders' investments. It is calculated by dividing net income by total equity.

Sixteen commercial banks are registered with the central bank of Nigeria, fourteen of these are quoted on the Nigerian Stock Exchange. Convenience sampling was employed, for availability of data the 14 quoted commercial banks were sampled for this study. Data were gathered for ten years (2008-2017) to capture long term effect as suggested by Toms, et al. [3]. 2008 being post-consolidated period and 2017 being the most recent year ended of audited and published full annual report. The gathered data resulted in 140 observations.

Validity and Reliability of Instruments

The major instruments for data collection, corporate annual reports of companies were carefully selected to include only audited annual reports, signed by reputable auditing firms. All the annual reports included in this study were qualified by the external auditor as representing a true and fair view of the affairs of the company. The researcher ensured that the annual reports included in the analysis were only those signed by the chairman of the board of directors of the reporting company. The gathered data was subjected to a normality test to determine whether the data set is well-modelled by a normal distribution or not. The D'Agostino-Pearson omnibus test for normality was carried out on the data.

MODEL SPECIFICATION

To test the hypothesis of this study, the regression model applied by Toms, et al. [3] was adapted in the following implicit function and regression equation:

$$\mathrm{SDQ} = f(\mathrm{ETS},\ \mathrm{POWS},\ \mathrm{SIZ},\ \mathrm{ROE}) \qquad (1)$$

$$\mathrm{ROE} = \beta 0 + \beta 1\ \mathrm{EDS} + \beta 2\ \mathrm{SDS} + \beta 3 \mathrm{GDS} + \beta 4\ \mathrm{GI} + \varepsilon \qquad (2)$$

Where:

$\beta 0$: Intercept

$\beta 1, \ \dots,\ \beta 4$: Coefficient of Slope Parameters

Ɛ: Error term.

ROE is Return on Equity representing financial performance.

EDS is Environmental disclosure.

SDS is Social Disclosure.

GDS is Governance disclosure.

GI is Gross income representing company size.

SDQ is proxied by environmental reporting quality (ERQ).

Social reporting quality (SRQ).

Governance reporting quality (GRQ).

RESEARCH HYPOTHESES

To achieve the objectives of this study, research hypotheses have been developed. Each hypothesis is stated in null and the alternate forms as follows:

1. **H0:** Corporate ethical standard does not have significant relationship with the quality of sustainability disclosures published by commercial banks in Nigeria.

H1: Corporate ethical standard has significant relationship with the quality of sustainability disclosures published by commercial banks in Nigeria.

2. **H0:** Corporate ethical standard has no significant impact on the quality of sustainability disclosures published by commercial banks in Nigeria.

H1: Corporate ethical standard has significant impact on the quality of sustainability disclosures published by commercial banks in Nigeria (Table 1).

Table 1: Descriptive Statistics.

	N	Minimum	Maximum	Mean		Std. Deviation	Skewness		Kurtosis	
	Statistic	Statistic	Statistic	Statistic	Std. Error	Statistic	Statistic	Std. Error	Statistic	Std. Error
Environmental Report Quality	140	1	5	2.35	0.103	1.223	0.546	0.205	-0.571	0.407
Social Report Quality	140	1	5	4.33	0.099	1.166	-1.857	0.205	2.49	0.407
Governance Report Quality	140	2	5	3.43	0.067	0.797	0.367	0.205	-0.304	0.407
Ethical Standard	140	-1	1	-0.03	0.085	1.003	0.058	0.205	-2.026	0.407
Return on equity	140	-0.225	0.997	0.245	0.029	0.346	-4.044	0.205	2.516	0.407
Power of Shareholders	140	0.001	0.96	0.210	0.023	0.280	1.497	0.205	0.934	0.407
Bank Size	140	0.03	512.4	145.2	0.019	118.5	0.883	0.205	0.274	0.407
Valid N (list wise)	140									

The maximum score obtainable for ESG reporting quality was achieved in the data set, in each of the three categories. Some of the analyzed reports scored the lowest mark for the reporting quality of environmental and social impacts while, corporate governance reporting quality was at least the score ‘2’, which means that all the reports analyzed in the sample had disclosure on corporate governance. For all the variables, the skewness revolves around 0 which means the data set is symmetrical and the kurtosis is of less than 3 shows the data set has a normal peak.

Normality Test

The histograms in Figures 1-3 show the normal distribution of the data det for the dependent variables of this study, that is, environmental reporting quality, social reporting quality and governance reporting quality.

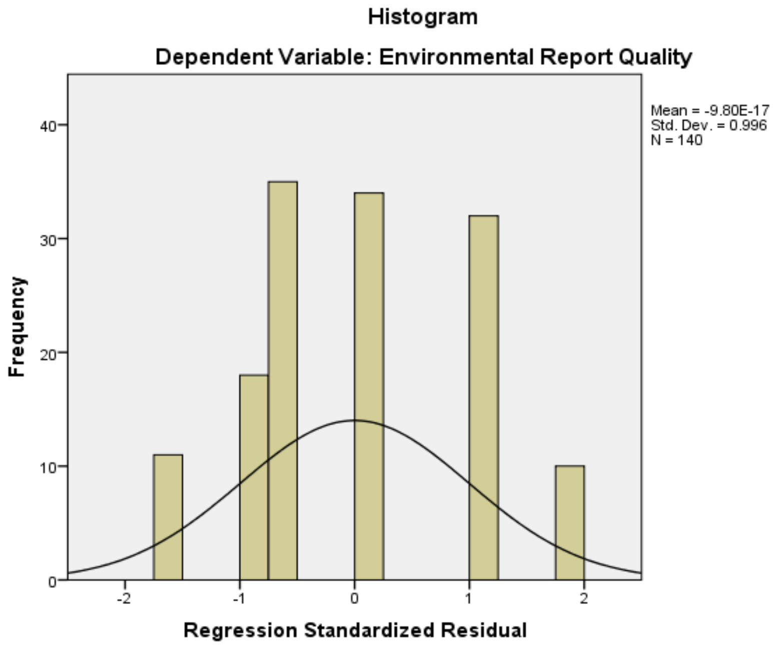

Figure 1: Environmental reporting quality.

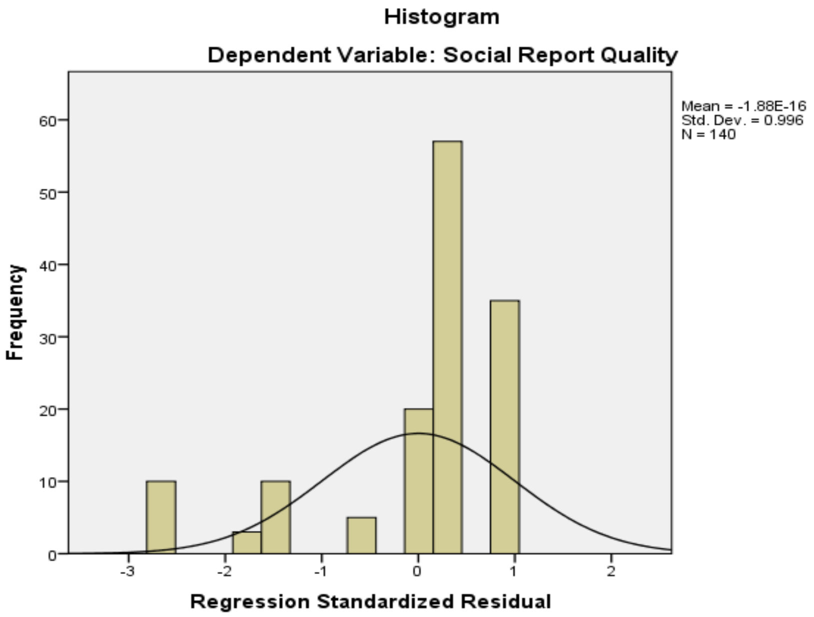

Figure 2: Social reporting quality.

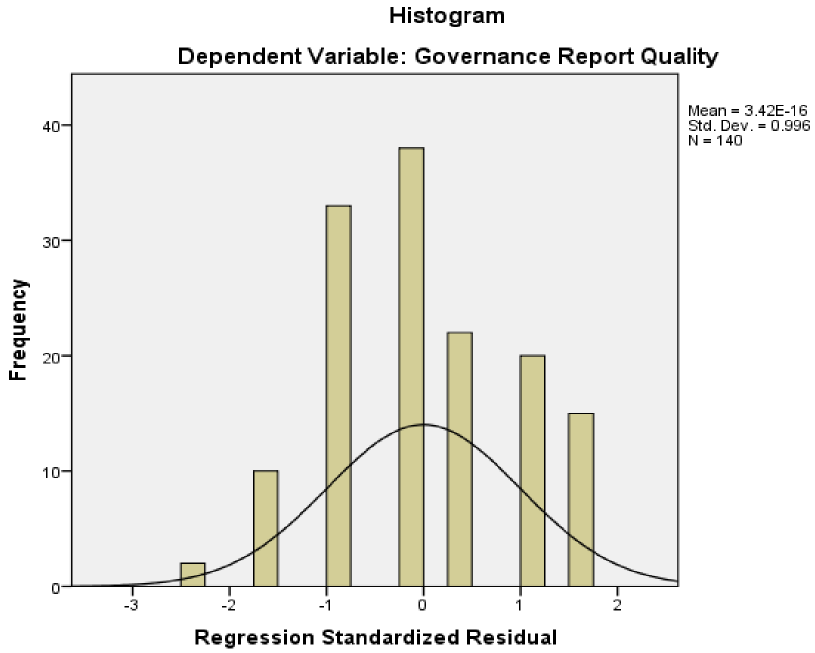

Figure 3: Governance reporting quality.

Table 2: Correlations.

		Environmental Report Quality	**Social Report Quality**	**Governance Report Quality**	**Ethical Standard**	**Return on equity**	**Power of shareholders**	**Bank size**
Environmental Report Quality	Pearson Correlation	1	0.237**	0.391**	0.455**	0.083	-0.224**	0.570**
	Sig. (2-tailed)		0.005	0	0	0.332	0.008	0
	N	140	140	140	140	140	140	140
Social Report Quality	Pearson Correlation		1	0.304**	.287**	0.015	0.043	0.138
	Sig. (2-tailed)			0	0.001	0.861	0.615	0.103
Governance Report Quality	Pearson Correlation			1	0.345**	0.131	-0.093	0.568**
	Sig. (2-tailed)				0	0.124	0.273	0

Ethical Standard	Pearson Correlation				1	-0.09	0.093	-0.326**
	Sig. (2-tailed)					0.292	0.275	0
Return on equity	Pearson Correlation					1	0.434**	0.316**
	Sig. (2-tailed)						0	0
Power of shareholders	Pearson Correlation						1	-0.304**
	Sig. (2-tailed)							0
Bank size	Pearson Correlation							1
	Sig. (2-tailed)							

Test of Hypotheses

- **H0:** Corporate ethical standard does not have significant relationship with the quality of sustainability disclosures published by commercial banks in Nigeria.
- **H1:** Corporate ethical standard has significant relationship with the quality of sustainability disclosures published by commercial banks in Nigeria.

The correlation table presents a coefficient of 0.455 between corporate ethical standard and environmental reporting quality (significant at 0.01 levels). Correlation coefficient between corporate ethical standard and social reporting quality is 0.287 (significant at the 0.01 level). The correlation coefficient between corporate ethical standard and governance reporting quality is 0.345 (significant at 0.01 levels). This result confirms that a relationship exists between corporate ethical standard and sustainability reporting quality. Therefore, the null hypothesis is rejected, and the alternate is accepted that corporate ethical standard has significant relationship with the quality of sustainability disclosures published by commercial banks in Nigeria.

Table 2 also includes the correlation between ethical standard and power of shareholders, which implies that there is a relationship between the ethical standard of a commercial bank in Nigeria and the investment decision of the bank's shareholders.

Hypothesis Two

H0: Corporate ethical standard has no significant impact on the quality of sustainability disclosures published by commercial banks in Nigeria.

H1: Corporate ethical standard has significant impact on the quality of sustainability disclosures published by commercial banks in Nigeria (Table 3).

Table 3: Between-Subjects Factors.

		Value Label	N
Ethical Standard	-1	litigation default	72
	1	no litigation default	68

Of the 140 corporate reports analyzed, 72 contained contingent liabilities arising from litigation while 68 had no such contingent liabilities (Table 4).

Table 4: Multivariate Tests[a].

Effect		Value	F	Hypothesis df	Error df	Sig.
Intercept	Pillai's Trace	0.86	271.339[b]	3	133	0
	Wilks' Lambda	0.14	271.339[b]	3	133	0
	Hotelling's Trace	6.12	271.339[b]	3	133	0
	Roy's Largest Root	6.12	271.339[b]	3	133	0
ROE	Pillai's Trace	0.043	1.972[b]	3	133	0.121
	Wilks' Lambda	0.957	1.972[b]	3	133	0.121
	Hotelling's Trace	0.044	1.972[b]	3	133	0.121
	Roy's Largest Root	0.044	1.972[b]	3	133	0.121
POWS	Pillai's Trace	0.052	2.409[b]	3	133	0.07
	Wilks' Lambda	0.948	2.409[b]	3	133	0.07
	Hotelling's Trace	0.054	2.409[b]	3	133	0.07
	Roy's Largest Root	0.054	2.409[b]	3	133	0.07
SIZ	Pillai's Trace	0.383	27.487[b]	3	133	0
	Wilks' Lambda	0.617	27.487[b]	3	133	0
	Hotelling's Trace	0.62	27.487[b]	3	133	0
	Roy's Largest Root	0.62	27.487[b]	3	133	0

	Pillai's Trace	0.192	10.525[b]	3	133	0
	Wilks' Lambda	0.808	10.525[b]	3	133	0
	Hotelling's Trace	0.237	10.525[b]	3	133	0
ETS	Roy's Largest Root	0.237	10.525[b]	3	133	0
[a]Design: Intercept + ROE + POWS + SIZ + ETS						
[b]Exact statistic						

Corporate ethical standard (ETS), Return on equity (ROE), Power of shareholders (POWS), and Bank size (SIZ) jointly and significantly impact the quality of sustainability reporting on commercial banks in Nigeria (Table 5).

Table 5: Tests of Between-Subjects Effects.

Source	**Dependent Variable**	**Type III Sum of Squares**	**df**	**Mean Square**	**F**	**Sig.**
Corrected Model	Environmental Report Quality	92.167[a]	4	23.042	26.889	0
	Social Report Quality	16.278[b]	4	4.069	3.183	0.016
	Governance Report Quality	31.338[c]	4	7.834	18.572	0
Intercept	Environmental Report Quality	107.292	1	107.292	125.208	0
	Social Report Quality	482.497	1	482.497	377.37	0
	Governance Report Quality	228.932	1	228.932	542.701	0
ROE	Environmental Report Quality	4.965	1	4.965	5.794	0.017
	Social Report Quality	0.038	1	0.038	0.03	0.864
	Governance Report Quality	0.098	1	0.098	0.232	0.631
POWS	Environmental Report Quality	5.773	1	5.773	6.736	0.01
	Social Report Quality	0.141	1	0.141	0.111	0.74
	Governance Report Quality	0.093	1	0.093	0.22	0.64
SIZ	Environmental Report Quality	32.697	1	32.697	38.157	0
	Social Report Quality	0.644	1	0.644	0.503	0.479
	Governance Report Quality	19.247	1	19.247	45.626	0
ETS	Environmental Report Quality	20.449	1	20.449	23.863	0
	Social Report Quality	11.164	1	11.164	8.732	0.004

	Governance Report Quality	2.157	1	2.157	5.114	0.025
Error	Environmental Report Quality	115.683	135	0.857		
	Social Report Quality	172.608	135	1.279		
	Governance Report Quality	56.948	135	0.422		
Total	Environmental Report Quality	981	140			
	Social Report Quality	2812	140			
	Governance Report Quality	1734	140			
Corrected Total	Environmental Report Quality	207.85	139			
	Social Report Quality	188.886	139			
	Governance Report Quality	88.286	139			
[a]R Squared=0.443 (Adjusted R Squared=0.427)						
[b]R Squared=0.086 (Adjusted R Squared=0.059)						
[c]R Squared=0.355 (Adjusted R Squared=0.336)						

From the adjusted R-squared of 42.7%, 5.9% and 33.6% it interprets that corporate ethical standard causes 42.7% change in environmental reporting quality, 5.9% change in social responsibility reporting quality and 33.6% change in corporate governance reporting quality of commercial banks in Nigeria. Therefore, the null hypothesis is rejected, and the alternate is accepted that corporate ethical standard has significant impact on the quality of sustainability disclosures published by commercial banks in Nigeria. The findings of this study agree with the research of Ramakrishan (2007) who confirmed the relationship between business ethics and corporate governance.

CONCLUSION

Based on the data analysis and findings of this work, the following conclusions are drawn:

- This research has proved that corporate ethical standard directly impacts the quality of sustainability reporting of commercial banks in Nigeria.

- There is a significant long-term effect as anticipated by the ten-year study. Environmental, social responsibility and governance disclosures improved over the years and their relationship with ethical standard became more significant in every additional time period.
- Disclosure on corporate governance policies and compliance is at a comparably higher quality than social responsibility disclosure and environmental disclosure. Social responsibility reporting practise in many Nigerian commercial banks mainly entails a list of donations while environmental reporting practice is basically policy statements. In most of the analysed reports environmental and social reports were combined under headings like 'Health, safety and environment (HSE)', 'Community Affairs, Safety, Health, Environment & Security (CASHES)'.
- The sustainability reporting practice of commercial banks in Nigeria could be greatly improved. There is a wide gap between the current sustainability disclosure quality and international standard of sustainability disclosure practice.

RECOMMENDATION

The following recommendations are offered:

- Voluntary disclosure of environmental preservation activities and social responsibility activities should be improved. The quality of sustainability reports published by the bank would present the bank as an ethical entity. This would influence the investment decisions of shareholders, as suggested by the findings of this work.
- Business and industry regulators need to educate managers and directors of commercial banks on sustainability accounting and reporting. This would help to improve the reporting quality.
- Regulators and leaders of the commercial banks should be equipped with relevant information on the social and environmental impacts peculiar with the nature of their business.
- Academic institutions in Nigeria should review their curriculum for accounting

courses to include subjects and topics that teach sustainability accounting and reporting so the Nigerian accountant would be well equipped for the job.

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