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An investigation of compliance with international accounting standards by listed companies in the Gulf Co-Operation Council member states

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Abstract

This study investigates the extent of compliance with international accounting standards (IASs) by companies in the Gulf Co-Operation Council (GCC) member states (Bahrain, Oman, Kuwait, Qatar, Saudi Arabia, and the United Arab Emirates). Based on a sample of 137 companies (436 company-years) we find that compliance increased over time, from 68% in 1996 to 82% in 2002. Despite strong economic and cultural ties between the GCC states, there was significant between-country variation in compliance and among companies based on size, leverage, internationality, and industry. The study provides evidence of de jure but not de facto harmonization in the region. Noncompliance reflected some ineffectiveness in the functions of external auditors and enforcement bodies, which may be of interest to countries that have adopted IASs recently.

Keywords: Adoption of International Accounting Standards (IAS); Financial-reporting compliance; Audit function; Enforcement of accounting standards; Gulf Co-Operation Council (GCC) member states

1. Introduction

Rapid globalization of financial markets has given rise to demands for more internationally comparable financial reporting. Harmonization of accounting is one way

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to promote more transparent and consistent reporting and to that end the International Accounting Standards Board (IASB) produces international accounting standards for use by private sector entities throughout the world. Since 2005 there has been widespread adoption of IASB standards on a mandatory basis. Consequently, there is increased interest in the comparability of reporting being achieved as well as the role of auditors and enforcement bodies in promoting compliance (SEC, 2000; CESR, 2003; Schipper, 2005).

The aim of this paper is to investigate the level of compliance over time with international accounting standards (IASs) in the six Gulf Cooperation Council (GCC) states, namely Bahrain, Oman, Kuwait, Saudi Arabia, Qatar, and the United Arab Emirates (UAE) and the factors associated with compliance. The GCC countries made IASs mandatory progressively since 1986 for some or all listed companies. This setting allows us to explore the use of IASs in a number of economically important developing countries, which were early adopters of IASs. Mandatory use in the GCC countries provides an opportunity to examine the role of external auditors and enforcement bodies in promoting compliance with IASs.

Using a self-constructed compliance checklist, we measure the extent of 137 listed companies' compliance with 14 relevant IASs over the period 1996–2002 (436 company-years).[1] For the GCC as a whole, the average level of compliance for all years was 0.75; for disclosure it was 0.69 and for measurement 0.81. The level of compliance increased over time in each state, with overall measures increasing from 0.68 in 1996 to 0.82 in 2002, indicating that compliance has been improving in the region.

Despite strong links between member states, compliance varies among them. Since diversity could reflect differences in each country's regulatory framework, we provide a self-constructed enforcement score (encompassing legal requirements, quality of the audit function, and activities of enforcement bodies) for each country. The highest average compliance level for all years is in the UAE (0.80), followed by Saudi Arabia (0.78), Kuwait (0.75), Oman (0.74), Bahrain (0.73) and Qatar (0.70). Differences in compliance levels are generally consistent with national enforcement scores. Compliance also varies by industry, being lower among financial-sector firms. It is higher for larger companies and those with higher leverage and a greater international presence.

Compliance with IASs has been measured in several settings in prior research. For example, disclosure compliance is reported in Australia (0.94; Tower, Hancock, & Taplan, 1999), Germany (0.81; Glaum & Street, 2003) and Switzerland (0.74; Street & Gray, 2001). Measurement compliance is reported for Germany (0.86) and Switzerland (0.92; Street & Gray, 2001). Our study adds to this literature in two significant ways. First, it considers countries from a developing region which has considerable economic and political importance but has been the subject of relatively little research. Prior studies, such as Abdelrahim, Hewaidy, and Mostafa (1997), Abdelrahim and Mostafa (2000) and Joshi and Al-Mudhahki (2001), have not examined compliance in depth, across countries and over time. Our study achieves this and provides empirical evidence about the progress of harmonization in the region. The results are, therefore, of interest to academics and practitioners following the development of more comparable financial reporting on a global scale.

[1] The compliance checklist is available from the corresponding author.