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IFRS compliance in GCC countries: Do corporate governance mechanisms make a difference?

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Abstract

This research aims at examining the level of International Financial Reporting Standards (IFRS) compliance across the entire Gulf Cooperation Council (GCC) region and seeks to explore the impact of corporate governance mechanisms on the level of compliance with IFRS disclosure requirements. We employ a cross-sectional analysis of 314 non-financial listed companies within the GCC countries. The compliance level with IFRS was measured using a self-built disclosure index consisting of 379 mandatory disclosure items of IFRS. The partial compliance method was implemented in calculating the compliance score for the targeted companies. The results show that none of the targeted companies had fully complied with the disclosure requirements of IFRS. Three corporate governance mechanisms were found to have a significant effect on the level of compliance with IFRS, namely board independence, concentrated ownership and the external auditor quality. Further, the results are not indicative of any distinctive contributions of board size, chief executive officer (CEO) duality, institutional ownership, audit committee size and the number of audit committee meetings held during the year on the level of compliance with IFRS. Hence, the current results may reflect that corporate governance best practices need to be revised to improve the level of compliance with IFRS, particularly in emerging markets. We draw out the implications for theory and practice.

Keywords: Corporate Governance; Compliance; IFRS; GCC; emerging markets.

Introduction

The call for adopting the International Financial Reporting Standards (IFRS) by regulators was motivated by several factors, such as avoiding the information asymmetry of stakeholders (Procházka, 2017), raising capital from foreign markets (El-Gazzar *et al*, 1999), decreasing the cost of obtaining information for decision makers (De George *et al*, 2013), and increasing market efficiency through emphasizing the reliability and relevance levels of accounting information (Jermakowicz and Gornik-Tomaszewski, 2006). Researchers have further reported that having a unified set of accounting standards best serves the needs of the public users of financial statements through decreasing the variations in the national accounting practices that resulted from the differences in the institutional and cultural dimensions among countries (Herath and Alsulmi, 2017). Moreover, implementing IFRS among countries was reported to have several benefits regarding enhancing capital markets' efficiency, facilitating cross border investments and improving the comparability and transparency of financial reporting (Nurunnabi, 2017).

The integration of world capital markets led to the worldwide harmonization of financial reporting through IFRS adoption. Pichler *et al* (2018) emphasized that internationalization and globalization are the most important motives of the harmonization of financial statements preparation and presentation. Hence, countries all over the world started to adopt IFRS either completely or partially during the last couple of decades, intending to reach for a common accounting language among companies (Klann and Beuren, 2018). The significant progress toward the convergence of accounting standards was with EU's decision that made the use of IFRS mandatory for the purpose of preparing consolidated financial statements starting from January 2005. The appropriate implementation of the disclosure requirements of IFRS is the most important challenge of achieving the desired accounting harmonization around the world (Yamani and Hussainey, 2021). Hence, with this rapid spread of IFRS adoption among countries, researchers started to investigate this phenomenon from several perspectives.

In more detail, research related to IFRS adoption was approached from three main strands. The first strand is related to examining a firm's level of compliance with disclosure requirements of the International Accounting Standards (IAS)/IFRS and the applicability of certain standards in a particular environment (Van Zijl and Maroun, 2017; Shimamoto and Takeda, 2020). The second strand of research focuses on investigating the factors that affect the level of IFRS compliance; scholars examined the impact of firms' characteristics (e.g., Bova and Pereira, 2012; Lin, 2012; Lopes *et al*, 2016), corporate governance variables (e.g., Krismiaji and Surifah, 2020) and institutional factors (e.g., Avwokeni, 2016; Alzeban, 2018) on the level of compliance with IFRS requirements. The third strand is related to examining the impact of IFRS compliance on several variables, such as the disclosure level (e.g., Aksu and Espahbodi, 2016), firms' value and foreign direct investment (e.g., De George *et al*, 2013), decision making (e.g., Chandrasekar and Kumar, 2016) and voluntary disclosure (Uyar *et al*, 2019; Akman, 2011).

This study comes within the first and second strands, as it first examines the level of IFRS compliance for the listed companies in all the Gulf Cooperation Council (GCC) countries (i.e., Saudi Arabia, Kuwait, Qatar, United Arab Emirates (UAE), Bahrain and Oman). Second, it examines the impact of corporate governance mechanisms on the level of compliance with IFRS; scholars attempted to examine the effect of corporate governance on the level of compliance with IFRS, standing on the fact that the former is essential in improving companies' transparency and accountability, which helps in improving managers' confidence of the users of financial statements (Verriest *et al*, 2013). In addition, improving corporate governance practices helps in enhancing the effectiveness of controlling and monitoring managers' performance, which leads to increasing the efficiency of companies' disclosure practices (Petra, 2007).

The GCC region is an appropriate platform to examine the impact of corporate governance on IFRS compliance, aiming to draw out implications that are applicable to other emerging markets. This could be attributed to several reasons; first, these countries have been investigated together in the literature because they have common political, social and economic features and they possess similar histories, cultures and traditions. They also share the same geographical area, religion, ethnicity and language, and the same economic conditions, as they rely on oil as a main source of income (Shehata, 2015). Therefore, it is expected to have similar corporate characteristics across all GCC countries at the accounting practices and corporate governance features levels, such as the dominance of the family-affiliation model of ownership (Al-Qahtani, 2005), the dominance of controlling shareholders as board members (Saidi, 2004) and the existence of a large number of state-owned corporations (Gulf News, 2017). Second, GCC countries are considered early adopters of IFRS; for example, Oman adopted IAS in 1986 and Kuwait in 1991 (Al-Mannai and Hindi, 2015). This would imply that they have high levels of experience in complying with the disclosure requirements of such standards. Third, although their awareness of corporate governance best practices is improving, they still face challenges in fully adopting such practices (Abdallah and Ismail, 2017).

The rest of the paper is structured as follows. The second section presents a review of the prior work that examined the effect of corporate governance on companies' disclosure practices and introduces the accounting and corporate governance practices in GCC countries. The third section demonstrates the deducted research hypotheses. The fourth section offers a discussion of the methods adopted for this research. The fifth section is dedicated to analyzing the data collected, and, finally, the sixth section provides the discussion and conclusions and draws out the implications for theory and practice.

Literature Review

IFRS Compliance

The importance of implementing IFRS has been evidenced through providing benefits that exceed the costs of complying with such standards (Bova and Pereira, 2012); these standards mainly aim to achieve a fair presentation of financial statements rather than legal compliance (Lin, 2012). The flexibility in adopting IFRS has increased the number of countries that have implemented IFRS (Tribuzi, 2018). Accordingly, scholars have become interested in examining the level of compliance with IAS/IFRS during the past couple of decades. For example, Street *et al* (1999) examined the level of compliance with IAS in 12 different countries for the year 1996 using a sample of 49 companies; they found a significant low level of compliance with IAS and reported that only 41% of the sampled companies complied with all IAS. Street and Gray (2002) used a larger sample of 279 firms in 32 different countries for the year 1998 and showed that the average compliance was 74%. Also, Glaum and Street (2003) compared the level of compliance with IAS and German Generally Accepted Accounting Principles (GAAP) for a sample of 200 companies in Germany for the year 2000; they found that the level of compliance for companies that use GAAP was 86.6% and 80.9% for the companies that implemented IAS. Fekete *et al* (2008) used a sample of Hungarian companies and stated that the level of compliance of these companies was 62% on average.

More recent studies have also reported similar results, such as Devalle *et al* (2016), who revealed a low level of compliance with the mandatory disclosure requirements of intangible assets for a sample of 189 Italian companies for the year 2010. Abdullah *et al* (2012), through testing the annual reports of public listed companies and meeting with accounting practitioners in Malaysia, found that none of the sampled companies fully complied with IFRS disclosure requirements. In another study, Edogbanya and Kamardin (2014) found a high level of compliance with IFRS by Nigerian financial institutions. Hasan *et al* (2013) also showed that the level of disclosure has been improved in Bangladeshi listed firms, but it is still below expectations. Furthermore, using a sample of 168 listed companies in Turkey for the year 2011, Demir and Bahadir (2014) stated that the level of compliance with IFRS disclosure requirements for these companies lay between 64% and 94% with an average of 79%.

Studies conducted in the Middle East and Gulf countries have also reported similar results. For example, Abdelrahim *et al* (1997) conducted a study on 22 Kuwaiti listed companies to examine the extent of the adoption of selected standards for the year 1995; they found that the companies fully complied with the mandatory requirements of these standards, but not with the voluntary ones. In the same context, Al Mutawaa and Hewaidy (2010) found that the overall compliance level was 69% for 48 listed companies in Kuwait for the year 2006. Alsaqqa and Sawan (2013) examined the effect of moving from the adoption of GAAP to IFRS in the UAE and reported that such adoption enhanced the relevancy, reliability, comparability and understandability of accounting reports. In Jordan, Omar and Simon (2011) reported that the level of compliance was 69%. In another work, Al-Akra *et al* (2010) found that the level of compliance with the mandatory disclosure requirements significantly increased through the period of study between 1996 and 2004 in Jordan. In Egypt, Dahawy and Conover (2007) stated that the level of compliance with the mandatory market requirements averaged 61%. Joshi and Al-Mudhahki (2013) used a sample of 37 listed companies in Bahrain and reported a fair level of adoption of IAS 1 disclosure requirements. Al-Jabri and Hussain (2012) stated that Omani listed companies did not fully comply with the requirements of IFRS, and the average level of compliance among the sampled companies was 79%. Al-Shammari *et al* (2008) attempted to examine the level of compliance with IFRS within the GCC member states for the period of 1996 to 2002 using a sample of 137 companies; they showed that the average level of compliance among all the sampled firms was 75%.

Corporate Governance and IFRS Compliance

The quality of information disclosed to shareholders is one of the most important aspects of corporate governance. It is held that effective corporate governance helps in reducing financial reporting problems and bad accounting outcomes (Hasan *et al*, 2013). Likewise, Verriest *et al* (2013) noted that the stronger the corporate governance, the more transparent the IFRS restatements. In France, Bouchareb *et al* (2014) found that adopting IFRS in 2005 and having good corporate governance practices decreased the level of earnings management. Marra and Mazzola (2014) also revealed that the effectiveness of corporate governance in decreasing earnings management is higher around the period of transition towards IFRS in Italian companies.

Similarly, Aboagye-Otchere *et al* (2012) reported that the level of mandatory disclosure in Ghana improved through the period of 2003−2007 due to the improvements in some corporate governance mechanisms. Chakroun and Matoussi (2012) stated that the composition of the board of directors had an influence on the level of voluntary disclosure for a sample of Tunisian firms for the period of 2003−2008. Luthan and Satria (2016) found that board independence and audit committees had a negative impact on earnings management before and after the period of convergence to IFRS in Indonesia. Further, using a sample of 50 top companies from Malaysia, Indonesia, Thailand and Singapore, Khan *et al* (2020) found a significant effect of some corporate governance mechanisms (i.e., board size, board expertise, board meetings and board diversity) on the quality of disclosure.

In the Middle Eastern context, both external and internal corporate governance mechanisms were found to play an efficient role in providing a high-quality level of voluntary disclosure in Saudi Arabia (Al-Janadi *et al*, 2013). In Turkey, Aksu and Espahbodi (2016) compared the level of transparency and disclosure between the voluntary adopters of IFRS during 2003−2004 and the mandated adopters in the year 2005; they revealed that the scores were significantly higher for the voluntary adopters.

Accounting Standards and Corporate Governance in GCC Countries

The adoption of IFRS in GCC countries started in 1986. Some of these countries required all listed companies to adopt IFRS, while other countries required listed companies in specific industries to adopt IFRS (Al-Mannai and Hindi, 2015). More specifically, in Oman, Kuwait and Bahrain, all listed companies were required to comply with IAS in 1986, 1991 and 1996, respectively. In Saudi Arabia, Qatar and the UAE, only banks and investment and financial firms were asked to comply with IAS in 1992, 1999 and 1999, respectively, as instructed by the central banks of these countries (Al-Shammari *et al*, 2008).

Huge efforts were made in GCC countries towards improving their corporate governance codes so that they could be aligned with the rapid growth of their capital markets (Qurashi, 2017). This was supported by the initiatives taken by the international institutions in helping the Middle East and North Africa (MENA) region in developing their own corporate governance codes. In 2005, the Hawkamah (an Arabic term for corporate governance) Institute was established to help the MENA region in developing and implementing integrated corporate governance frameworks to overcome the governance gap. The main objective of Hawkamah is to "shape corporate governance practices and framework throughout the region by promoting the core values of transparency, accountability, fairness, disclosure, and responsibility" (Shehata, 2015, p: 317). Another major role of Hawkamah is engaging different governments and industries in forming various corporate governance benchmarks that may be considered motives in enhancing corporate governance practices in the region (Qurashi, 2017).

The first corporate governance code issued was in Oman in 2002, and the most recent code was in Kuwait and Bahrain (Husseinali *et al*, 2016). Regarding board composition, all six GCC countries require at least one third of the directors to be independent, and the role of board chairman and the chief executive officer (CEO) must be separate. For board size, only Bahrain and Saudi Arabia had determined the number of board members; Bahrain's code in particular determined that the number of board members should not be more than 15 members, while Saudi Arabia's code requires the number of members to be not less than 3 and not more than 11. Additionally, all codes require the presence of an audit committee formed mostly from non-executive members (Abdallah and Ismail, 2017).

Hypotheses Development

Board Independence

Agency theory suggests that non-executive directors can monitor and control the activities of other board members, which enhances the board's control function and improves its performance, making it more efficient (Singh et al., 2018). Outside directors monitor the flow of disclosed information, which increases the disclosed information and decreases the level of information asymmetry of stakeholders (Kelton and Yang, 2008). Resource dependency theory looks at the outside directors as a channel to link the company with the external environment and assist it in getting its needed resources, as they are expected to have more knowledge and experience since they may be working in different industries. Researchers that have examined the relationship between board independence and financial disclosure have revealed mixed results. While some studies have found the level of disclosure to be positively related to the proportion of independent directors (e.g., Agyei-Mensah, 2017), others found it to be negative or with no significant relationship at all (e.g., Hasan *et al*, 2013). Accordingly, our first hypothesis is as follows:

H1: *There is a significant positive relationship between board independence and the extent of compliance with IFRS disclosure requirements in GCC member states.*

Board Size

As stated by the agency theory, the number of board members increases its monitoring function and strategic decision-making effectiveness (see Singh *et al*, 2017). It further suggests that the possibility of having dominant managers decreases when having a large number of board members (Samaha *et al*, 2012). Additionally, resource dependency theory looks at large boards as a tool to provide the company with more experience and more knowledge, which is considered an enhancement in its monitoring and controlling functions (Haniffa and Cooke, 2002). Existing studies, including those conducted in the Middle East region, have revealed mixed results. For instance, Ezat and El-Masry (2008) and Al-Janadi *et al* (2013) found board size to be positively related to the degree of disclosure in Egypt and Saudi Arabia, respectively, while other studies did not report any significant relationship on this matter (e.g., Samaha *et al*, 2012).

Based on the theoretical argument stated above, our second hypothesis is as follows:

H2: *There is a significant positive relationship between board size and the extent of compliance with IFRS disclosure requirements in GCC member states.*

Chief Executive Officer (CEO) Duality

The separation between the CEO position and board chair position was supported by the agency theory to avoid the concentration of authority in the hands of one person (Hashim and Devis, 2008). It supports the idea that the separation between the two positions enhances the latter's independence, where the independent chairman can efficiently oversee and monitor management's activities (Al-Janadi *et al*, 2013). The resource dependency theory also argues that having a CEO from outside the company links it with the resources needed from the external environment and brings to it external prospects, which help in achieving its goals and objectives (Dahya and Travlos, 2000). Empirically, the existing results on CEO duality and disclosure are somewhat contradictory. For instance, some scholars (e.g., Allegrini and Greco, 2013; Marra and Mazzola, 2014) have claimed the relationship to be positive, while others have not (e.g., Ahmed *et al*, 2006; Petra, 2007).

Overall, it is anticipated that holding the chairman of the board and the CEO positions by the same person will limit the efficiency and the independence of monitoring and controlling the activities of the company's managers; hence, the third hypothesis is as follows:

H3: *There is a significant negative relationship between CEO duality and the extent of compliance with IFRS disclosure requirements in GCC member states.*

Ownership Structure

We included two types of ownership structure: concentrated ownership and institutional ownership. Dumontier and Raffournier (1998) suggested that IFRS compliance may be considered a monitoring activity for shareholders and a bonding activity for managers. However, the high level of ownership concentration is expected to enhance the monitoring power of shareholders over the company's management as shareholders with large ownership percentages have more incentives to track the company's performance and its strategic decisions. Lee and Yeh (2004) suggested that the probability that mangers will utilize the company's resources in their own interests is higher in companies with dispersed ownership. Additionally, the conventional predictions of the agency theory would expect that the existence of institutional shareholders would enhance the level of compliance with IFRS, as their presence would mitigate the agency problem through pushing companies to disclose more information to reduce the level of the information asymmetry (Donnelly and Mulcahy, 2008). Prior studies have not reached at a definite conclusion regarding the relationship between ownership structure and the level of disclosure. For example, Gao and Kling (2012) and Ballas *et al* (2018) concluded a positive relationship between the two variables, while Pichler *et al* (2018) concluded a negative relationship. To examine both stated variables of ownership, we formulated the following two hypotheses:

H4a: *There is a significant positive relationship between concentrated ownership and the extent of compliance with IFRS disclosure requirements in GCC member states.*

H4b: *There is a significant positive relationship between institutional ownership and the extent of compliance with IFRS disclosure requirements in GCC member states.*

Audit Committee

This committee plays a crucial role in advising and supporting the board of directors in major accounting issues, in the preparation of financial statements and in ensuring that these statements were prepared in accordance with the accounting rules and regulations (Brennan, 2007). It is also considered a formal communication channel between board members, internal control systems and the external auditor (Bradbury *et al*, 2006). The number of meetings held by the audit committee is considered an indication of its diligence (Kelton and Yang, 2008). The number of audit committee members and meetings were found to be effective mechanisms for determining the disclosure level (Kelton and Yang, 2008; Allegrini and Greco, 2013). Al-Shammari and Al-Sultan (2010) reported that the existence of an audit committee has a positive relationship with voluntary disclosure. However, Al-Janadi *et al* (2013) and Sellami and Fendri (2017) did not find a significant relationship between audit committee effectiveness and the level of disclosure.

For the purpose of this work, the effect of audit committee effectiveness on the level of compliance with IFRS was measured by two dimensions: the number of audit committee members and the number of audit committee meetings. Hence, we propose the following two hypotheses:

H5a: *There is a significant positive relationship between the number of audit committee members and the extent of compliance with IFRS disclosure requirements in GCC member states.*

H5b*: There is a significant positive relationship between the number of audit committee meetings held during the year and the extent of compliance with IFRS disclosure requirements in GCC member states.*

External Auditor

Agency theory suggests that the existence of the external auditor is considered a tool to minimize the agency cost through reducing the level of information asymmetry between insiders and outsiders (Barako *et al*, 2006). This stands on the idea that the quality of the external auditor plays an important role in determining the level of disclosure and in providing a reasonable assurance to shareholders that financial statements were prepared in accordance with accounting rules and regulations (Brennan, 2007). Moreover, the ability of the external auditor to detect material errors in the financial statements affects the extent of the disclosed information (Gao and Kling, 2012). Scholars have concluded that companies audited by one of the big-four audit companies experienced a higher level of disclosure and higher level of compliance with IFRS (e.g., Pichler *et al*, 2018). However, Depoers (2000) and Barako *et al* (2006) revealed that the quality of the external auditor did not contribute to the level of disclosure in their studies. Therefore, the last hypothesis was stated as follows:

H6: *There is a significant positive relationship between the quality of the external auditor and the extent of compliance with IFRS disclosure requirements in GCC member states.*

Research Methodology

Data and Sample

Data was collected from the annual reports of the listed companies in the stock exchanges of the six GCC member states; the inclusion of these countries stands on the fact that all their listed companies are implementing IFRS in preparing their financial statements and they are obliged to follow corporate governance rules issued by the Organization for Economic Cooperation and Development (OECD). The data collection process lasted for almost a year; we started collecting data in October 2018, targeting 2017 financial statements. However, at that time, 30%–40% of the annual reports of the targeted companies were not available for 2017. Therefore, the required data was collected for 2016 in an attempt to include all the listed companies in the analysis. Hence, the study population comprises the 450 non-financial listed companies at the end of the fiscal year on 31 December 2016. Financial institutions, such as banks and insurance companies, were excluded due to their different nature and because their disclosure practices are governed by the central bank's requirements and regulations (Abed *et al*, 2012). In an attempt to arrive at generalized conclusions, we decided to target the entire population rather than selecting a specific sample. Nevertheless, due to the unavailability of data, the final analysis included 314 companies out of the 450. Table 1 shows the distribution of the targeted companies within GCC countries and industry sectors.

TABLE 1 ABOUT HERE

Variables Measurement

Outcome Variable (IFRS Compliance)

To measure and quantify the level of compliance with the mandatory disclosure requirements of IFRS, we implemented a self-built disclosure index. Marston and Shrives (1991) illustrated that a well-constructed disclosure index is considered to be a reliable and convenient tool for measuring the degree of companies' compliance with IFRS. Implementing a disclosure index is justified by the following. First, it is the most common tool adopted by prior work to measure the extent of disclosure (see, for example, Haniffa and Cooke, 2002; Tsalavoutas, 2011). Second, it supports providing a single figure that summarizes the whole content of the company's annual report, which helps easily detect the variations in the disclosure practices among companies (Marston and Shrives, 1991). Third, it helps in quantifying the presence of an information item, which makes it possible to clearly and objectively operationalize the extent of disclosure (Marston and Shrives, 1991).

Notably, as the existing literature indicates, no single common disclosure index is used by scholars and no theory governs the number and selection of the standards that should be included in the disclosure index (Barako *et al*, 2006; Hassaan, 2012). Disclosure indices that were previously implemented were built depending on the research purposes, research design and the relevance and applicability of the disclosure requirements within the research context. Therefore, following is a discussion of the criteria implemented in selecting the IFRS and disclosure requirements to be included in the disclosure index checklist and the steps followed to calculate the level of compliance with IFRS.

<u>Selecting IFRS</u>

We focused on all the mandatory disclosure requirements in the financial statements and in the notes of these statements of the 42 standards issued by IASB until the end of 2016. However, our review excluded some standards as they were inapplicable to the research focus and context. The final disclosure index included 27 standards compromising 379 disclosure items. The disclosure index was divided into sub-indices, as each sub-index represents the mandatory disclosure requirements of a particular standard. Such a disclosure index encompasses some standards that were ignored and excluded by most of the previous studies due to the nature of the country's labour laws, namely IAS 19 (Employees Benefits) and IAS 26 (Accounting and Reporting by Retirement Benefits Plans). However, after an extensive review of these standards, it was concluded that they are not applicable in some of the MENA region contexts, but they are applicable to others, particularly GCC countries, and thus, they were included in the current research, as recorded in Table 2.

TABLE 2 ABOUT HERE

Scoring the disclosure items

Based on the un-weighted approach of disclosure items, scoring the disclosure index was completed following the prior work (see, for example, Al-Htaybat, 2005), where each disclosure item is coded 1 if the required disclosure was done by the company and 0 if the disclosure item is applicable but was not disclosed. Disclosure items that were not applicable for the company were coded as NA (not applicable), and they were dropped from the scoring system of the company. To mitigate the uncertainty in scoring the disclosure index and to avoid penalizing the company for not disclosing a non-applicable item, the entire company's annual report was carefully reviewed, which enabled an understanding of the nature of the company's operations and helped in determining the applicability of the disclosure items to the company (Cooke, 1989a, 1989b). Thereby, if a disclosure item was not found in the annual report and it was not mentioned in the auditor's annual report, it was assumed to be not applicable (Glaum and Street, 2003).

Calculating the level of compliance with IFRS

Two methods could be applied in calculating the level of compliance with IFRS disclosure requirements; these are the dichotomous method and the partial compliance method. The number of the required disclosure items significantly varies among the standards; hence, to avoid assigning different weights to the standards, we employed the partial compliance method (see Tsalavoutas *et al*, 2010). Following this method, the total level of compliance with IFRS was calculated by adding the level of compliance of each standard, which gives equal weighting to each standard. In more detail, the total level of compliance of each standard was separately calculated, and then the results of all the standards were added together to get the total compliance. This total was divided over the total number of applicable standards for the company. Based on this, the degree of compliance was expressed as a percentage ranging from 0 if the company did not disclose any item for all the standards to 1 if it disclosed all items for all the applicable standards.

The calculation of the compliance level (disclosure index) for each company is as follows:

$PC = \frac{\sum X}{R}$,

where

PC is the total compliance score for a company ($0 \leq PC \leq 1$);

X is the level of compliance of each standard; and

R is the number of applicable standards for a company.

Independent Variables

<u>Corporate governance mechanisms</u>

This section highlights the measurement of the corporate governance mechanisms that were previously discussed, as shown in Table 3.

TABLE 3 ABOUT HERE

Control Variables

Following prior work and based on the availability of data, we considered a number of firm characteristics as control variables: firm size, profitability, liquidity, leverage and industry type. In regard to measuring the industry type variable, it was noticed that each country had applied its own classification (sectors) for companies; for example, Kuwait had identified 10 sectors, Oman had 17 sectors, whilst Bahrain had 4 sectors. Therefore, we compiled all the existing sectors in these countries; hence, five industry types were included, namely investment, industrial, services, energy and real estate. Table 4 presents the measurement of these control variables.

TABLE 4 ABOUT HERE

Research Model

The model that was constructed to examine the effect of corporate governance on the level of compliance with IFRS disclosure requirements is as follows:

$$COMP_{it} = \propto_0 + \beta_1 INDEP_{it} + \beta_2 BSIZE_{it} + \beta_3 SEPAR_{it} + \beta_4 CONCEN_{it} + \beta_5 INST_{it} + \beta_6 ACMEM_{it} + \beta_7 ACMEET_{it} + \beta_8 EXTAUD_{it} + \beta_9 FSIZE_{it} + \beta_{10} PROFT_{it} + \beta_{11} LEV_{it} + \beta_{12} LIQ_{it} + \beta_{13} IND\_INV_{it} + \beta_{14} IND\_INDS_{it} + \beta_{15} IND\_SER_{it} + \beta_{16} IND\_ENE_{it} + \beta_{17} IND\_RST_{it} + \varepsilon_{it},$$

where

$COMP_{it}$*: the level of compliance with IFRS.*

$INDEP_{it}$*: the number of independent outside directors over the total number of board members.*

$BSIZE_{it}$ *: the number of board members.*

$SEPAR_{it}$ *: a dummy variable that equal zero if the CEO also acts as the chairman of the board of directors and 1 otherwise.*

$CONCEN_{it}$ *: the percentage of shares owned by major shareholders.*

$INST_{it}$ *: the percentage of shares owned by major institutional shareholders.*

$ACMEM_{it}$ *: the number of audit committee members.*

$ACMEET_{it}$ *: the number of audit committee meetings held during the year.*

$EXTAUD_{it}$ *: a dummy variable that equals 1 if the external auditor is one of the BIG-FOUR and 0 otherwise.*

$FSIZE_{it}$ *: the natural logarithm of the total assets.*

$PROFT_{it}$ *: is the Return on Assets (ROA) ratio.*

LEV_{it}, : *the firm leverage which is calculated by dividing the total debts over the total assets.*

LIQ_{it} *: the firm liquidity measured by the current ratio.*

IND_INV_{it} *: a dummy variable equals 1 if the company operates in the investment sector and 0 otherwise.*

IND_INDS_{it}*: a dummy variable equals 1 if the company operates in the industrial sector and 0 otherwise.*

IND_SER_{it},*:a dummy variable equals 1 if the company operates in the services sector and 0 otherwise.*

IND_ENE_{it} *: a dummy variable equals 1 if the company operates in the energy sector and 0 otherwise.*

IND_RST_{it} *: a dummy variable equals 1 if the company operates in the real state sector and 0 otherwise.*

Data Analysis and Results

Regression Analysis

As shown in table 5, the variance inflation factor (VIF) values indicate that no multicollinearity is evident (Hair *et al*, 2010). Hierarchical multiple regression analysis was used to examine the effect of corporate governance mechanisms on the level of compliance with IFRS. Table 5 also presents the results of the regression analysis of the model. In the first step, the control variables were entered, namely firm size, profitability, liquidity, leverage, investment, services, energy and real estate, with all corporate governance mechanisms entered afterward to examine their impact on the level of compliance with IFRS.

TABLE 5 ABOUT HERE

Having controlled firms' characteristics, the value of R^2 of IFRS compliance was calculated ($R^2 = .17$, $p < .001$). The results show that corporate governance mechanisms explained a strong significant incremental level of variance in R^2 in addition to what controls were explained in IFRS compliance ($\Delta R^2 = .10$, F for ΔR^2 4.598, $p < .001$). Further, the F-ratio is considered as an indication of the goodness of the model in predicting the outcome variable (Field, 2018). Given the fact that the F-ratio is highly significant ($p < .001$), it was concluded that the model is able to explain the changes in the outcome variable. Moreover, the results show that the value of R^2 is close to the value of adjusted R^2, which supports the potential generalizability of the results. The difference between the two numbers was not significant (.17−.125 = .045); this implies that if the model was run for the entire population rather than a selected sample, about 4.5% less variance in IFRS compliance would be shown.

The industry type was determined in five groups as a classification of the type of company's operations, which resulted in five dummy variables; thus, one of these dummy variables must be excluded from the regression analysis. The excluded dummy variable was treated as the baseline and a reference group. Therefore, the industrial sector was excluded when running the multiple regression analysis, as it represented the majority and allowed for comparisons with other groups (see Field, 2018).

As recorded in table 5, a significant positive relationship was observed between board independence and IFRS compliance ($\beta = .119$, $t = 2.108$, $p < .05$), which supports our first hypothesis. Hypothesis 2 suggested a positive relationship between board size and IFRS compliance, but the respective coefficient was not significant ($\beta = -.074$, $t = 1.189$, $p > .05$), which means that hypothesis 2 was not supported. The results regarding hypothesis 3 that predicted a negative relationship between CEO duality and IFRS compliance were also not significant ($\beta = .044$, $t = .812$, $p > .05$); hence, hypothesis 3 was rejected. Hypothesis 4, which suggested a positive relationship between ownership structure and IFRS compliance, was divided into two sub-hypotheses; hypothesis 4a suggested a positive relationship between concentrated ownership and

IFRS compliance; this hypothesis was supported as the coefficient was positive and significant ($\beta = .240$, $t = 2.031$, $p < .05$). The second sub-hypothesis was 4b, which proposed a positive relationship between institutional ownership and IFRS compliance; the results show a non-significant effect of institutional ownership on the level of compliance with IFRS ($\beta = -.067$, $t = .570$, $p > .05$). Hence, hypothesis 4b was disapproved. Hypothesis 5, which looked at the existence of a positive relationship between audit committee effectiveness and IFRS compliance, was also divided into two sub-hypotheses. The first hypothesis (5a) was rejected, as the results showed a non-significant impact of audit committee size on the level of compliance with IFRS ($\beta = .069$, $t = 1.186$, $p > .05$). Similarly, hypothesis 5b was not supported, implying that the number of audit committee meetings held during the year does not affect the level of compliance with IFRS ($\beta = -.006$, $t = -.107$, $p > .05$). Finally, regarding hypothesis 6, which suggested that the quality of the external auditor has a positive effect on IFRS compliance, the results provide a highly significant positive relationship between the quality of the external auditor and IFRS compliance ($\beta = .181$, $t = 2.901$, $p < .01$); thus, hypothesis 6 was approved.

Discussion and Conclusions

This is a study of the impact of a number of corporate governance mechanisms on the level of compliance with IFRS within the GCC region. The results reveal a number of interesting findings. We found that independent members are effective in enhancing the level of compliance with IFRS. Such results conclude that independent members in GCC listed companies are effective in handling their responsibilities in regard to properly monitoring and controlling mangers' disclosure actions. This may be attributed to the proposition of the agency theory suggesting that independent members play a major role in reducing the information asymmetry between managers and shareholders as they monitor the flow of disclosed information (see Kelton and Yang, 2008). Moreover, the resource dependency theory looks at those directors as a channel to link the company with outside resources because they have more relations, knowledge and experience (Barako *et al*, 2006).

Concentrated ownership was also reported to have a significant positive relationship with IFRS compliance. Such results could be explained by the notion that the high level of concentration of ownership increases the monitoring power of shareholders over managerial decisions. Hence, shareholders with a high percentage of shares are motivated to track their company's performance and its strategic decisions more than other shareholders with a lower percentage of shares (Brennan, 2007). Moreover, as suggested by the coercive isomorphism perspective, companies' disclosure practices are affected by their major stakeholders due to the pressure that the latter put over managers' decisions, as managers usually take into consideration the needs and desires of large shareholders (O'Sullivan *et al*, 2008).

The results revealed that companies being audited by one of the big-four audit companies have a higher level of compliance with IFRS. The quality of the external auditor plays an important role in determining the level of disclosure and providing a reasonable assurance to shareholders that the financial statements were prepared in accordance with accounting rules and regulations (Brennan, 2007). The size of the external auditor's firm influences the disclosure practices implemented by companies, and the latter contributes to the idea that big audit firms have more resources and experience that are needed to encourage their clients to have higher levels of compliance with IFRS in comparison with small audit firms (Demir and Bahadir, 2014). Large audit firms have more clients; therefore, they are less dependent on them in comparison with small audit firms. This gives the former a greater chance to exert pressure to force their clients to disclose more information (Owusu-Anash, 1998).

However, the existence of non-significant relationships with the other corporate governance mechanisms (board size, CEO duality, institutional ownership and audit committee effectiveness) indicate the relative inapplicability of the propositions of the agency theory and the resource dependency theory regarding their effect on the level of compliance with IFRS. Therefore, the following discussion will be based on the articulations of the institutional theory to justify our findings.

Scholars have argued that some context-related factors, such as the enigmatic culture of some emerging markets, influence the level of IFRS adoption (Chau and Gray, 2002). Unlike developed nations, companies operating in developing countries are somewhat less encouraged to disclose more information; instead, they tend to maintain such information exclusively to the insiders of the company (Haddad *et al*, 2015). Emerging markets in general and the GCC region in particular can be characterized by a lack of solid institutional building, where existing institutional arrangements are fluid and underdeveloped (Haak-Saheem *et al*, 2017). Therefore, the aforementioned propositions and the absence of specific and clear requirements of the optimum size of the board within the GCC region resulted in the lack of a significant relationship between board size and the level of compliance with IFRS. Similarly, such intuitional factors in emerging markets' settings may affect the awareness about the importance of separating the CEO position and the board chairman position in improving the latter's independence. Therefore, the separation between these two positions seems not to achieve its desired benefits in enhancing the board's monitoring and controlling functions over managers' behaviours. Companies may segregate the two positions only to gain legitimacy and to show that they are applying the rules of corporate governance, but without an effective activation of this important feature.

Institutional investors may access their companies' information by more efficient and timely ways to obtain value relevant information (Donnelly and Mulcahy, 2008). In other words, they can obtain information from sources other than the financial statements, such as formal meetings with management. Donnelly and Mulcahy (2008) noted a crucial difference between the information released in annual reports and the information released in formal meetings. Hence, the existence of these shareholders does not affect the level of compliance with IFRS, as it does not affect their abilities of getting their needed information about the company.

Audit committee was found to be not effective in monitoring the disclosure practices of the company. In other words, audit committee in emerging markets is not acting in line with the intended benefits and desires of its existence as the diligence of the audit committee plays an important role towards monitoring and controlling the best disclosure practices (Allegrini and Greco, 2013). Additionally, increasing the number of meetings will increase its ability to spot and resolve the divergences in accounting and financial issues between management and the external auditor (Pucheta-Martínez and De Fuentes, 2007).

Implications for Theory and Practice

This work confirms the relative applicability of some of the institutional theory's propositions within the GCC context. The absence of the impact of a number of corporate governance mechanisms on the level of compliance with IFRS may be explained by the fact that national culture is responsible for forming the level of compliance with IFRS. In other words, the cultural backgrounds of the financial statements' preparers and users are responsible in determining the level of awareness and understanding of the importance of implementing the disclosure requirements of IFRS in improving the transparency of the financial statements (Saudagaran and Meek, 1997). Such results further support the cultural dimensional model provided by Gray, (1988), which states that companies in developing countries prefer secrecy over transparency of their financial statements and they tend to keep information only for internal users.

With regard to the agency theory, the separation between ownership and control in developing countries needs to be more recognized by their listed companies. Also, the effectiveness of the monitoring function of the board of directors over managers' actions still needs to be enhanced. This was proven by the absence of significant effects of board size and audit committee effectiveness on the level of compliance with IFRS. Additionally, despite the fact that most of the targeted companies had separated the CEO position and chairman of the board position, there was a lack in the awareness of the importance of such a practice, which was evidenced by the lack of a significant relationship between CEO duality and the level of IFRS compliance.

We also offer a number of implications for practice; the findings provide a better understanding for policy-makers and regulatory agencies in relation to corporate governance practices of the listed companies in the GCC region. Some companies did not comply with the corporate governance codes issued in these countries; therefore, it is suggested that their regulatory bodies may carry out additional corporate governance reforms to enhance public awareness about the importance of corporate governance in improving the disclosure practices for companies and to ensure that listed companies are applying corporate governance best practices. The latter is mostly applicable in the case of existing problematic standards which have demonstrated a low level of compliance across all targeted companies within the GCC region, namely, IAS 19 and IAS 26.

Moreover, board independence had a significant positive impact on IFRS compliance. This result suggests that the existence of the independent members on a board have a significant role in improving the level of compliance with IFRS disclosure requirements. Therefore, this provides a recommendation for policy-makers and regulators in the GCC region to increase the proportion of independent members on the board of their listed companies to be the majority of the board rather than only one third, which is currently the case.

Increasing the number of audit committee meetings that must be held during the year is also recommended. This would be expected to enhance the diligence of such a committee and to help its members to more effectively track the disclosure practices and the implementation of IFRS disclosure requirements by their companies. Further, increasing the number of members on the audit committee would help improve their monitoring role, enhance their ability to oversee companies' financial reporting practices and work as a linking channel between managers and the external auditor. Finally, our findings on concentrated ownership and the level of compliance raises the need to increase the awareness of small investors about their companies' procedures that had been implemented in disclosing financial information. They need also to recognize their rights to ask management to comply with the disclosure requirements of IFRS to improve the transparency of the financial statements.

Limitations and Future Work

Despite our contributions, we acknowledge a number of limitations. First, we only targeted the non-financial listed companies within GCC countries; financial institutions were not included due to the different rules and regulations that govern their disclosure practices. Hence, future work could encourage financial institutions to provide some comparative lessons in relation to the level of compliance between financial and non-financial institutions. Moreover, the cross-sectional design did not allow the establishment of causal links among the variables of interest (Darwish *et al*, 2016); hence, future work could employ a longitudinal design to establish causal relationships and to mitigate the time-lag effect on the relationship between both corporate governance and IFRS compliance. Finally, other mechanisms of corporate governance were not included in this work, such as the educational background of the board members and the independence of the audit committee members. Such variables are worth further investigation, particularly within emerging markets.

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Table 1 Distribution of targeted companies among GCC countries/ sectors

Across Countries							
Country	Saudi Arabia	Kuwait	UAE	Oman	Qatar	Bahrain	Total
No. of listed companies	108	49	49	69	26	13	314
Across Sectors							
Sector	Investment	Industrial	Services	Energy	Real State	Total	
No. of listed companies	38	134	78	24	40	314	

Table 2 Number of disclosure items for each standard included in the disclosure index[1]

Standard	Title	No. of disclosure items
IAS 1	Presentation of Financial Statements	101
IAS 2	Inventories	9
IAS 7	Statement of Cash Flows	14
IAS 10	Events After Reporting Period	4
IAS 11	Construction Contracts	9
IAS 16	Property, Plant and Equipment	20
IAS 17	Leases	6
IAS 18	Revenue	7
IAS 19	Employees Benefits	11
IAS 21	The Effects of Change in Foreign Currency Rates	3
IAS 23	Borrowing costs	3
IAS 24	Related Party Disclosure	14
IAS 26	Accounting and Reporting by Retirement Benefit Plans	23
IAS 33	Earnings Per share	4
IAS 36	Impairment of Assets	16
IAS 37	Provisions, Contingent Liabilities and Contingent Assets	14
IAS 38	Intangible Assets	22
IAS 40	Investment Property	29
IFRS 2	Share-based Payment	4
IFRS 7	Financial Instruments: Disclosure	54
IAS 32	Financial Instruments	
IFRS 9	Financial Instruments	
IFRS 8	Operating Segments	9
IFRS 12	Disclosure of Interest in Other Entities	3
IAS 28	Investment in Associates and Joint Ventures	
IFRS 10	Consolidated Financial Statements	
IFRS 11	Joint Arrangements	
Total		**379**

[1] Some standards are qualifying standards; even that they are obligatory for companies to be implemented, they do not include any presentation or disclosure requirements. Specifically, the disclosure related to IAS 28 (Investment in Associates and Joint Ventures), IFRS 10 (Consolidated Financial Statements), and IFRS 11 (Joint Arrangements) are under IFRS 12 (Disclosure of Interest in Other Entities). Likewise, the disclosure requirements of financial instruments of IAS 32 (Financial Instruments) and IFRS 9 (Financial Instruments) were moved to IFRS 7 (Financial Instruments: Disclosure).

Table 3 Measurements of corporate governance mechanisms

Independent Variable	**Measurement**
Board Independence	The percentage of the independent outside directors from the total number of directors
Board Size	The total number of board members
CEO Duality	A dummy variable was used, if there is a separation between CEO and chairman roles the company was coded 1, and 0 otherwise.
Concentrated Ownership	The total percentage of shares owned by major shareholders (shareholders who own more than 5% of the total shares)
Institutional Ownership	The percentage of shares owned by major institutional shareholders (institutions who own more than 5% of the total shares).
Audit Committee Size	The total number of audit committee members
Audit Committee Meetings	The total number of audit committee meetings held during the year
External Auditor Quality	A dummy variable was used by coding the company 1 if the external auditor is one of the big-four audit companies around the world, and 0 otherwise.

Table 4 Measurements of control variables

Variable	**Measurement**
Firm Size	The logarithm of the total assets
Profitability	Return on Assets Ratio (ROA)
Liquidity	Current ratio, which was calculated by dividing current assets over current liabilities.
Leverage	The total debt to assets ratio through dividing the total liabilities over total assets.
Investment	A dummy variable is coded 1 if the company belongs to investment sector and 0 otherwise
Industrial	A dummy variable is coded 1 if the company belongs to industrial sector and 0 otherwise
Services	A dummy variable is coded 1 if the company belongs to services sector and 0 otherwise
Energy	A dummy variable is coded 1 if the company belongs to energy sector and 0 otherwise
Real estate	A dummy variable is coded 1 if the company belongs to real state sector and 0 otherwise.

Table 5 Hierarchical regression analysis for IFRS compliance

	Step 1		Step 2		VIF
Variables	**B**	**Sig.**	**B**	**Sig.**	
Controls					
Firm Size	.029	.630	.057	.404	1.645
Profitability	.026	.668	.004	.943	1.311
Liquidity	.028	.672	.033	.599	1.411
Leverage	.244	.001	.207	.003**	1.735
Investment	.087	.147	.072	.232	1.305
Services	.104	.090	.063	.312	1.371
Energy	-.070	.240	-.112	.063	1.283
Real Estate	.063	.302	.054	.369	1.294
Corporate Governance					
Board Independence			.119	.036*	1.134
Board Size			-.074	.235	1.402
CEO Duality			.044	.417	1.054
Concentrated Ownership			.240	.043*	4.979
Institutional Ownership			-.067	.569	4.995
Audit Committee Size			.069	.237	1.207
Audit Committee Meetings			-.006	.915	1.186
External Auditor			.181	.004**	1.397
R^2	.067 (.042)		.17 (.125)		
ΔR^2	.067		.103		
F for ΔR^2			4.598***		
Durbin Watson	2.067				

Note: N=314. Industrial sector is the omitted benchmark sector.
Adjusted R^2 is in parentheses
*$p < .05$, **$p < .01$, ***$p < .001$.