THE SUCCESS OF IFRS IN AFRICA: COMPARATIVE EVIDENCE BETWEEN GHANA AND KENYA

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ABSTRACT

Comparability of financial statements in the face of increased globalisation of businesses has triggered mandatory adoption of IFRS by many countries in the world. Kenya adopted IAS now IFRS in 1998 while Ghana adopted IFRS in 2007. This study empirically sought to determine the extent of compliance with IFRS in Ghana and Kenya and further determined whether significant difference exist between the two countries. The study also sought to determine company attributes that have a relationship with IFRS compliance rate in Ghana and Kenya. Financial reports of 31 companies listed on the Ghana Stock Exchange and 50 companies listed on the Nairobi Stock Exchange were examined and compliance scored with an aid of a checklist. The study revealed an overall compliance rate of 97.1% and 74.5% between Kenya and Ghana respectively. Pearson product moment correlation revealed company attributes of auditor type, Industry type and Internationality as variables having a positive association with IFRS compliance rate in both Kenya and Ghana. The study concluded that the differential attribute of Kenya having an older Stock Exchange and having adopted IFRS far earlier could explain its higher compliance over Ghana.

INTRODUCTION

The ever increasing focus on international standards cannot be over emphasized because of the vital end product of accounting "Financial Statements" which are used in assessing performance of companies. Those who have funds to invest or lend may decide where to place resources based on the financial reports. According to Mueller, Gernon & Meek (1997), providers of capital provide resources to business enterprise who are required to turn provided resources into productive use to maximize the interest of resource providers, and because ownership is separated from the business, resource users owe the responsibilities of providing a feedback in the form of financial statements to resource providers to determine how their investment has been maximized. This underscores the importance of accounting standards which regulates the preparation of financial statements to enhance reliability as a fundamental quality of accounting information.

Prior to the 1970's the development of accounting standards was customized to each country to meet the needs of its business environment. Differences in standards came about as a result of differences among countries with factors such as culture, legal systems, providers of finance,

taxation, accounting profession and inflation Choi and Mueller (1992); Nobes (1998); Radebaugh and Gray (1997) and Doupnik and Salter (1995).

However the unprecedented increase in foreign investment, the formation of regional economic groups such as (European Union and ECOWAS) and the growing need of multinational companies to raise capital for their operations in the stock market intensified the need for internationally accepted accounting standards to enhance the quality of financial information Radebaugh and Gray (1997). Eventually International accounting standards were developed in 1973 by a standard setting body called International Accounting Standard Committee whose functions were taken over by International Accounting Standard Board (IASB) in April 2001 with the authority to make the standards which is now termed International Financial Reporting Standards (IFRS) mandatory among its members (ACCA 2008, IAS Plus 2010).

The primary objective of the IFRS is to help companies generate general purpose financial statements that provide users with relevant, reliable and timely information (IASC Foundations 2009). It is argued by Imhoff (2003) that such information contributes towards the achievement of orderly capital markets around the world. Since the global implementation of IFRS over one hundred countries have adopted the standards with more other countries preparing to converge their standards to IFRS (Hibbard, 2012).

Kenya with the most vibrant and largest stock exchange in East Africa which was established in 1954 (IMF 2012), was the first to adopt IFRS in the sub region (World Bank 2001). The Nairobi Stock Exchange established in 1954 has the longest history and by far the largest in the sub region. It has 55 listed companies, reaching market capitalization of 46% of GDP as of 2010 (IMF 2012). The Council of Institute of Certified Public Accountants of Kenya adopted IAS now IFRS in 1998 and required all listed companies to comply even though it was not backed by law. However in 2001 the capital markets Authority of Kenya made it mandatory for all listed companies to comply (Outa, 2011; World Bank, 2001).

Ghana, a West African country had it stock exchange established in 1990 under the Stock Exchange Act of 1971 (Act 384), (Ghana Stock Exchange, 2011) and was the first to adopt IFRS in the West African sub region in its effort to deepen its commitment in expanding the private sector. The Council of the Institute of Chartered Accountants Ghana (ICAG) realising the significant gaps in the Ghana National Accounting Standards (GNAS) onwards, resolved to migrate from using the GNAS as the financial reporting framework to IFRS. Consequently Ghana adopted IFRS in 2007 requiring all companies listed on the Ghana Stock Exchange to comply.

Since the adoption of IFRS, there has been a number of empirical evidence of non compliance by companies even though they claim full compliance with IFRS in their financial reports (Larson & Street, 2004; Tsalvoustas et al., 2010; Lucchase & Di Carlo, 2012; Fekete et al. (2008). According to paragraph 16 of IAS 1 revised, entities shall not describe financial statements as complying with IFRS unless they comply with all the requirements of IFRS. Little studies have been conducted in this regard in Africa and no comparative studies have been identified in Africa though there have been a number of comparative studies in the developed countries. This study sought to compare the extent of compliance in Kenya with that of Ghana and to determine

whether any statistical difference exists. It also sought to compare company attributes associated with the extent of compliance. The choice of Ghana and Kenya was informed by the following reasons:

a) Both countries are Anglophone Countries colonized by Britian.
b) Both countries are the first to adopt IFRS in their respective sub-regions.
c) Both countries have the most vibrant stock exchange in their respective sub-regions.

LITERATURE REVIEW

Chatham (2008) noted that earlier research on IFRS compliance assumed that a firm's attestation regarding their use of IAS in the financial statements were enough to conclude that the firms are complying with the IASC/IASB standards making IFRS compliance dichotomous measure. For instance Dumonitier and Raffournier (1998) classified Swiss firms in the IAS group if it has declared that its financial statements conform to IAS. Ashbaugh and Pincus (2001) also assessed IAS compliance with a dichotomous measure to investigate the impact of IAS on the ability of analysts to accurately forecast earnings. They concluded that the adoption of IAS improved the analysts' ability to forecast earnings as it secures a reduction in the absolute value of analyst forecast errors.

Researchers have begun using sophisticated methods for measuring the degree of compliance with IFRS. Cairns (1999a) used a detailed measurement scale by placing firms into eleven compliance categories. Cairns found that there is significant non-compliance among sampled firms and concluded that firms' auditors confirmed companies compliance while there were obvious deviations. However Chatham (2008) pointed out several difficulties in using cairns (1999a) categorical approach by emphasising that the guidelines for placing a firm into a particular category seem less precise and more subjective for an empirical research.

The use of compliance index has been used by many researchers in assessing compliance with IFRS (Tower et al., 1999; Street & Bryant, 2000; Street & Gray, 2001; Glaum & Street, 2003; and Ballas& Tsovas, 2010) and has not yet received any criticism.
Street Bryant (2000) examined the extent to which seventeen countries complied with IAS. They found that non-compliance was significant with respect to IAS 8, 12, 17, 19, 23, and 33. They also sought to identify whether there were significant differences between companies with (1) a US listing (2) a US filling and (3) no US listing or filling, with regard to compliance with IAS disclosure. ANOVA results revealed significant differences between the three groups with respect to the level of compliance.

Glaum and Street (2003) investigated the extent to which companies listed on the German "Neuer Market" comply with IASs and US GAAP disclosure requirements. Using a sample of 100 companies whose financial reports are based on IAS, they reported an average compliance of 8% with 42% and 100% being the minimum and maximum compliance score respectively. Using OLS regression, they also revealed a positive association between level of compliance and companies audited by the "Big Five" Audit Firms while other attributes were insignificant. This finding is consistent with Patton and Zelenka (1997) who found a positive association in Czech Republic, and Al-Shammari (2011) also reported a positive association in Kuwait but incongruent with Naser 1995who reported a negative association in Hong Kong.

Alfaraih (2009) undertook an empirical study of compliance with IFRS and value relevance of accounting information in emerging stock markets in Kuwait. He measured compliance by a self constructed checklist focusing on the financial statements of 163 firms 2006 annual reports. The findings revealed significant variations in compliance levels among the selected standards with majority of the selected standards having intermediate compliance between 60% and 80% and overall mean compliance of all firms being 72.6%. According to Alfaraih a possible reason for this variation is the degree of difficulty associated with the application of the standards. The study further revealed that Profitability, Auditor Type, Leverage and Industry Type significantly influence the rate of compliance between companies.

A number of other studies have highlighted company attributes that influence the compliance level in accordance with IFRS. Popular among these attributes are Company Size, Profitability, Auditor Type, Leverage , Industry Type and Internationality. However results of relationship between these attributes and IFRS compliance have been divergent. Ballas and Tzovas (2010); Joshi and Almudhaki (2001); Ali Ahmed and Henry (2004); Bonson and Escobor (2001) found a significant positive relationship between Company Size and level of compliance while Street and Gray (2001) and Street and Bryant (2000) found no evidence of association.

Owusu Ansah (1998) and Patten and Zelenka (1997) reporterd a significant positive relationship between profitability and extent of IFRS compliance but Inchausti (1997) and Dumonitier and Raffournier (1998) reported a contrary result. A positive correlation between Auditor Reputation and IFRS compliance was evidenced by Bonson and Escobar (2006) and Gorgan and Gorgan (2012) while Naser (1995) found a negative correlation.

Al-Shammari (2011) reported that company attributes of Internationality, Industry Type, and Leverage associates positively with IFRS compliance. However Adjei-Mensah (2012); Ali et al. (2004) and Walace and Naser (1995) did not provide support for Leverage; Wallace et al. (1994) and Street and Bryant (2000) found no evidence of an association between type of Industry and IFRS compliance rate.

Based on the above review of literature the study tested the following hypothesis:

H1: There is a statistically significant difference between Ghana and Kenya with regard to their IFRS compliance ratio.

H2: There is a positive correlation between Company Size and rate of IFRS compliance in Ghana and Kenya.

H3: Profitability is positively associated with rate of IFRS compliance in Ghana and Kenya.

H4: Auditor Type is positively correlated with rate of IRS compliance in Ghana and Kenya.

H5: Industry Type is associated positively with IFRS compliance rate in Ghana and Kenya.

H6: There is a significant positive correlation between Internationality and IFRS Compliance rate in Ghana and Kenya.

H7: There is a positive correlation between leverage and rate of IFRS compliance in Ghana and Kenya.

METHODOLOGY

Population and Data Source

Financial reports of thirty one companies listed on the Ghana Stock Exchange and fifty companies listed on the Nairobi Stock Exchange as at 31st January 2011 whose financial statements claimed compliance with IFRS were used in the studies. In effect eighty six companies' financial reports were used. Data was obtained from 2010 financial statements of the eighty six companies using a self developed checklist with reference to IFRS issued by IASB (IASC Foundations, 2009) and checklist published by Deloitte (2010). This is consistent with Mutawaa and Hawaidy (2010) and Al-Shammari (2011). The checklist was developed for each of the selected standards (IAS 1, IAS 7, IAS 12, IAS 16, IAS 18 and IAS 19). The choice of standards was informed by their importance and applicability to all companies irrespective of the industry of operation. Each company was scored 'one' for an item disclosed and Zero for an item that ought to have been disclosed but not disclosed, consistent with Marfo-Yiadom and Atsunyo (2014).

Measurement of Dependent Variable

The rate of compliance being the dependent variable was measured by a compliance index (CI) in line with prior research by (Fekete, Matis & Lukas 2008; Amoako & Asante 2012). Compliance Index for each company was calculated by the equation: CI = AD/RD
Where AD = Actual Disclosure
RD = Required Disclosure
The compliance index ranges from the minimum of 0 representing no compliance to the maximum 1 representing full compliance with IFRS disclosure requirements. In effect a higher ratio depicts a high rate of compliance by a company.

Measurement of Dependant Variables

Independent variables used in this study are Company Size measured by book value of equity consistent with Ballas and Tzovas (2010); Profitability measured by return on equity (ROE) in line Naser et al (2002); Auditor Type measured by a dummy variable coded 1 if audited by the Big Four Auditing firms and coded 0 otherwise consistent with Makihija and Patton (2004); Internationality measured by a dummy variable coded 1 if affiliated with a parent company in the developed countries and 0 otherwise consistent with Meek et al. (1995) ; Industry Type measured by dummy variable with each industry given a numerical identification in line with Al-Shamari (2011); while leverage was measured by debt to equity ratio in line with Adjei Mensah (2012).

Data Analysis

Independent sample t-test was used to analyse hypothesis 1 while Pearson Product Moment Correlation was used in analysing hypothesis 2 to 7.

RESULTS AND DISCUSSION

Table 1: Independent Sample t-test on IFRS Compliance Rate between Listed Companies in Ghana and Kenya

Variables	Category	N	Mean	Std. Dev.	t-value	p-value	η^2
IFRS Compliance Ratio	Ghana	31	0.745	0.082	-11.875	0.000	0.641
	Kenya	50	0.971	0.084			

Source: Field data, 2016 Where η^2 = eta square **p < 0.01 (N = 81)

Independent sample t-test was used to analyse the data in order to test hypothesis 1 formulated. The result in Table 1 shows that there is a statistically significant difference at 0.01 significance level with regards to the level of IFRS compliance ratio in the mean values between listed companies in Ghana (Mean = 0.745, Std. Dev. = 0.082) and that of Kenya (Mean = 0.971, Std. Dev. = 0.084), [t = -11.875, df = 79, p < 0.01]. Beyond reaching statistical significance, the actual difference in mean values between listed companies in Ghana and Kenya were very large. The effect size, calculated using eta squared, were 0.641. The results show that the compliance rate of IFRSs presentation and disclosure requirement by listed companies in Kenya is higher than listed companies in Ghana. This means that listed companies in Kenya comply with IFRSs presentation and disclosure requirement than Ghanaian listed companies.

Thus, the p < 0.05, means that there is enough evidence to accept hypothesis 1 that there is a statistically significant difference between listed companies in Ghana and Kenya with regard to their IFRS compliance rate. According to the guidelines proposed by Cohen (as cited in Cohen, Manion & Morrison, 2007), interpreting the eta squared value means that, effect size is very large, because 64.1 percent of the variance in listed companies in Ghana and Kenya respectively could be explained by their IFRS compliance rate.

This result could imply that early adoption of IFRS by Kenya as well as the older age of its Stock Exchange accounts for its better compliance rate than Ghana.

Table 2: Relationships between IFRS Compliance rate and Company Attributes

	Rate of IFRS Compliance (Ratio)			
	Listed Companies in Ghana		Listed Companies in Kenya	
Variables	Correlation coefficient (r)	p-value	Correlation coefficient (r)	p-value
Size (Book Val. of Equity)	0.448*	0.011	0.022	0.882
Profitability (ROE)	0.225*	0.022	0.062	0.671
Auditor Type	0.454*	0.011	0.556**	0.003
Industry Type	0.495**	0.001	0.560**	0.001
Internationality	0.185*	0.016	0.438*	0.014
Leverage (Debt/equity)	-0.290	0.113	0.061	0.674
Rate of IFRS Compliance	1		1	

Source: Field data, 2016 *p < 0.05; **p < 0.01 (N_1 = 31; N_2 = 50; N = 81)

As contained in Table 2, company attributes such as company size, profitability, auditor type, industry type and internationality have statistically significant positive relationship with

companies' rate of IFRS compliance in Ghana. However, leverage was not related significantly to the listed companies in Ghana with regard to IFRS compliance rate. With regard to Kenya, auditor type, industry type, and internationality are statistically significant with IFRS compliance rate.

Specifically, the results in Table 2 indicates that company size as measured in terms of book value of equity is positively related to the rate of compliance with IFRSs presentation and disclosure requirements in Ghana but not in Kenya. Book value of equity was statistically significant at a significant level of 0.05. The results mean that company size have a strong statistically significant positive relationship with IFRS compliance rate in listed companies in Ghana ($r = 0.561$, $p < 0.05$) but not significant in listed companies in Kenya ($r = 0.067$, $p > 0.05$). These results imply that the larger the size of a company in Ghana, the higher the rate of compliance with IFRS, while no such correlation exists in Kenya. The positive association in Ghana is congruent with the results of Ballas and Tzovas (2010) who found a positive relationship between IFRS compliance rate and firm size. The result of no relationship established in Kenya is in agreement with street and Gray (2001) and Street and Bryant (2000) who found no evidence of association. Based on the finding, the study failed to accept the hypothesis that there is a statistically significant positive relationship between company size and rate of IFRS compliance in Ghana and Kenya.

Similarly, with regard to profitability which was measured by ROE, there was no statistically significant relationship between it and IFRS compliance ratio in listed companies in Kenya ($r = 0.051$, $p > 0.05$), but in relation to Ghana there was a statistically significant relationship ($r = 0.235$, $p < 0.05$). The relationship was weak but positive in nature. This shows that listed companies in Ghana with larger profits do have statistically significant higher levels of compliance with IFRS presentation and disclosure requirement while those with lower profit have lower level of compliance consistent with the study by Patten and Zelenka (1997). However, in the case of Kenya it does not matter a firms profitability to determine its compliance with IFRSs consistent with the results of Dumontier and Raffournier (1998). Again, the study rejects the hypothesis that profitability is positively associated with rate of IFRS compliance in Ghana and Kenya significantly.

However, there was a statistically significant moderate and positive relationship between auditor type and IFRS compliance rate of companies listed in both Ghana ($r = 0.454$, $p < 0.05$) and Kenya ($r = 0.556$, $p < 0.01$). The results mean that listed companies in Ghana and Kenya audited by one of the big four audit firms (PricewaterhouseCoopers, Deloitte & Touche, Ernst & Young, and KPMG) have a high level of compliance with the IFRSs disclosure requirements than those that were not audited by any of the big four firms. This results corroborates the outcome of the research by Bonson and Escobar (2006) and Gorgan and Gogan (2012). Therefore, the results fail to reject the hypothesis 4 that, listed companies in Ghana and Kenya audited by one of the big four (auditor type) do have statistically significant positive correlation with the level of compliance with IFRSs disclosure and presentation requirement.

Table 2 further shows that there is a strong statistically significant positive relationship between the types of industry and the level of company compliance with IFRSs disclosure requirement in both Ghana ($r = 0.495$, $p < 0.01$) and Kenya ($r = 0.560$, $p < 0.01$). This means that the type of

industry a company belongs, to a large extent relate to the level of compliance with the IFRSs disclosure requirements in both Ghana and Kenya. Based on the results, the study accepts the hypothesis that industry type is associated positively with IFRS compliance rate in Ghana and Kenya significantly and is congruent with the results reported by Al-Shammari (2011) but incongruent with results by Wallace et al. (1994) and Street and Bryant (2000) who found no evidence of association.

In relation to internationality, as indicated in Table 2, the result indicates that there is a statistically significant positive relationship between internationality and the level of company compliance with IFRSs disclosure requirement in Ghana ($r = 0.185$, $p < 0.05$) and Kenya ($r = 0.438$, $p < 0.05$). Both relationships are positive; however, the relationship between the two variables in Ghana was weak while that of Kenya was moderate. This shows that the more listed companies in Ghana and Kenya are affiliated with parent companies in any of the developed countries, the higher their level of compliance with the IFRSs disclosure requirements. Therefore, the study accept hypothesis 6 that there is a statistically significant positive correlation between internationality and IFRS compliance rate in Ghana and Kenya which is consistent with the results of Al-Shamari (2011).

The last company attributes considered was leverage which was measured by Debt to Equity ratio. Table 2 indicates that there are non-statistically significant relationships between leverage and the level of company compliance with IFRSs presentation and disclosure requirement in Ghana ($r = -0.290$, $p > 0.05$) and Kenya ($r = 0.061$, $p > 0.05$). Meaning that, debt to equity ratio (leverage) does not relate to listed companies rate of compliance with IFRS disclosure requirements in Ghana and Kenya. The study therefore rejects the hypothesis that there is statistically positive correlation between leverage and rate of IFRS compliance in Ghana and Kenya which is consistent with Ali et al. (2004) and Adjei-Mensah (2012).

CONCLUSION AND RECOMMENDATION

The study revealed a significant difference in compliance rate with IFRS between Ghana and Kenya. Kenya recorded a higher compliance rate of 97.1% as compared to Ghana which scored a compliance rate of 74.5%. The study also revealed Auditor Type, Industry Type, and Internationality as company attributes having a positive association with IFRS compliance rate in Ghana and Kenya. However Size and Profitability are additional company attributes that positively associates with IFRS compliance rate in Ghana but not Kenya. This performance in compliance with IFRS by Ghana and Kenya suggest that African countries which have adopted IFRS are significantly making progress towards full compliance with IFRS though a significant gap still exists. The study also concludes that the differential attribute of Kenya having an older Stock Exchange and having adopted IFRS far earlier could explain the its higher compliance over Ghana.

Given the criteria by IASB that companies should only claim compliance with IFRS in their financial reports only when they fully comply, the study recommends that the Security and Exchange Commission of both countries should intensify their monitoring to serve as a panacea for full compliance with IFRS.

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