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Compliance with IFRs: The case of risk disclosure practices in Egypt

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ABSTRACT

This study investigates the factors underlying non-compliance with IFRSs in Egypt. Evidence for this research was collected and analyzed using semi-structured interviews with academics, auditors, financial managers and officers in the Capital Market Authority, the Egyptian Exchange and the Egyptian Institute of Directors. Findings highlight the negative impact procedures-oriented accounting education, insufficient role of the profession in monitoring the professional performance of auditors, lack of adequate continuing education, the focus of the Unified Accounting System on bookkeeping with little importance of disclosure. Finally, competitive disadvantage is a significant threat to the reporting practices of Egyptian companies.

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1. Introduction

The International Accounting Standards Board (IASB), and its predecessor the International Accounting Standards Committee (IASC), has played an important role in harmonizing accounting practices through formatting and publishing accounting standards that underpin the preparation and presentation of financial statements (Nobes, 2002). In supporting this effort, the International Organization of Securities Commissions recommended the acceptance of International Financial Reporting Standards (IFRSs) by its members (Decker & Brunner, 2003, chap. 12). Despite the wide adoption of IFRSs, empirical research provides evidence of non-compliance.

According to Chen and Zhang (2010), since IFRSs are mainly adequate for highly developed capital markets its use in developing and emerging economies is questionable. Consequently, compliance with the requirements of IFRSs will be a major concern for those countries since the lack of financial reporting infrastructure, such as regulatory enforcement, may cause a significant non-compliance with IFRSs. The adoption of IFRSs may not enhance the accounting practice especially in developing countries that lack an organized accounting profession and regulatory authorities that support compliance with IFRSs (Chen & Zhang, 2010).

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Egypt is one of the important countries in the Middle East region and has strong economic ties with many countries in the world. Egypt is a relevant example to the cultural values represented in the Middle East region. Therefore, the result of this study may assist other countries in the region to enhance compliance with IFRSs. Since the early 1990s, The Egyptian government adopted significant restructuring plans of the economy and aimed to activate the Egyptian stock exchange.

The Egyptian government realized that sound corporate financial reporting and the adoption of IFRSs are necessary requirements for the success of its privatization program adopted in the early 1990s (ROSC, 2002). However, the preparation of Egyptian Accounting Standards (EASs) that are based entirely on the IFRSs ignores the fact that IFRSs are based on the Anglo/American approach to financial reporting and reflects Western societal values (Flower, 1997). Therefore, EASs do not reflect the nature of Egyptian societal values (El-Rashedy, 2006) and results in potential conflict between the disclosure requirement of IFRSs/EASs and the secrecy as a dominant accounting value in Egypt (El-Rashedy, 2006; Dahawy & Conover, 2007).

Empirical evidence has noted that Egyptian companies implement IFRSs selectively (Dahawy, Merino, & Conover, 2002) or with low level of compliance (Abd-El salam & Weetman, 2003). These studies support the need to understand the reasons behind the non-compliance with IFRSs on an individual basis. Although a number of studies examined compliance with IFRSs in Egypt (Abd-El salam & Weetman, 2003; Dahawy et al., 2002; Dahawy & Conover, 2007) none of these studies examined the factors that affect that compliance. This low level of compliance may be due to language barriers (Abd-El salam & Weetman, 2003), a conflict between secrecy as an accounting value and IFRSs disclosure requirements (Dahawy et al., 2002; Dahawy & Conover, 2007). According to Samaha and Khelif (2016), the evidence regarding the role of enforcement in compliance with accounting standards in emerging economies is not sufficient. Regarding risk reporting, Mokhtar and Mellett (2013) indicate that Egyptian companies provide backward-looking and qualitative risk disclosure and the level of compliance with mandatory risk reporting is rather low. This research responds to the call of Mokhtar and Mellett (2013) to examine the key reasons for non-compliance with mandatory risk reporting in Egypt.

Fueled by the debate in previous studies, this paper is motivated by the need for an in-depth understanding of the factors that threaten the compliance with IFRSs is important to assist accounting standard setters and regulatory bodies, such as the IASB, to support international acceptance of the IFRSs (Street & Gray, 2002). Therefore, this paper aims to address this gap in the literature by exploring the reasons that impede compliance with disclosure requirements in Egypt. Specifically, the study intends to answer the following question:

Why do Egyptian companies include less information in their financial reports?

This paper contributes to the literature by addressing why the adoption of IFRSs may not improve accounting practices especially that research in this area is very limited (Chen & Zhang, 2010). It addresses an important void in the literature by highlighting the reasons behind the low compliance with accounting disclosure requirements, especially risk disclosure in under-investigated developing countries context.

The rest of this article is organized as follows: after the introduction, section 2 describes accounting education and practice problems in developing countries. Section 3 discusses accounting education in Egypt. Section 4 presents the research design of this paper. Section 5 discusses the key findings related to the factors influencing disclosure in Egypt. Finally, section 6 presents the discussion and conclusion.

2. Accounting education and practice problems in developing countries

Developing countries are the focus of a limited number of accounting research that examine accounting education and practice problems. Because of their interdependence, accounting education has a significant role in enhancing accounting practice through providing qualified and competent accounting graduates (Tiggos, 1987). In addition, accounting research aims to identify the potential impact of these problems on compliance with mandatory and presentation of voluntary disclosure requirements. Accounting education and practice problems are a threat to reporting; a topic that requires a very high accounting skills and knowledge.

Several accounting studies highlight the problems that have been impact on accounting education and practice in developing countries while other studies aim to propose several strategies that may assist in overcoming these problems.

McGee (2006) argues that the successful implementation of IFRSs requires convincing practitioners and managers that the new requirements should be learned and applied, continuing professional education and upgrading the accounting curricula of universities. He highlighted the factors that may hinder the adoption and implementation of IFRSs in transition economies. He identifies four potential factors namely, low power of audit firms to force their clients to apply IFRSs due to the fear of losing clients, bookkeeping-oriented accounting, the tax authority employ tax standards rather than IFRSs to determine tax liability and translation problems because some English expressions, did not have any local counterparts.

Accounting education programs and accounting research are separated and are not directed to the economic objectives of developing countries. Akathaporn, Novin, and Andolmohammadi (1993) investigate the factors that may impede accounting education and profession development in Thailand. They identify several reasons that negatively affect the development of accounting education and the profession. The respondents recognize the irrelevance of the accounting curricula, shortage of qualified instructors and the lack of updated accounting textbooks as the main reasons for accounting education problems. In addition, the respondents point out that managers of Thai companies have very little accounting knowledge and consider accounting necessary only for tax purposes. Furthermore, the respondents highlight the lack of punishment mechanism and lack

of cooperation between academics and practitioners as potential reasons that hinder the development of accounting education, the profession and hence accounting practice in Thailand.

Other studies highlight the importance of continuing education, practical training of accounting students and cooperation between the profession and universities in education and research as potential strategies to overcome the problems of accounting education and practice in developing countries. Continuing education programs will assist practitioners to cope with the fast changing requirements of their duties (Tipgos, 1987). In addition, practical training for accounting students in their undergraduate studies will assist them to apply accounting knowledge in real world situations (Lin & Deng, 1992). Furthermore, cooperation between the profession and universities will assist in discussing real world problems and will provide the essentials inputs to conduct relevant academic research (Al-Basteki, 2000; Akathaporn et al., 1993).

Accounting literature documents the low level of compliance with mandatory disclosure (Akhtaruddin, 2005; Marston & Robson, 1997; Patton & Zelenka, 1997). However, few accounting researchers identify the factors that may impede compliance with and presentation of mandatory and voluntary disclosure. As McGee (2006, p. 202) pointed out “adopting IFRSs is one thing. Implementing them is something else. The mere fact that a government might adopt new accounting rules does not mean that they will be swiftly, efficiently and comprehensively applied and implemented throughout the economy.”

This is the case in Egypt since the mere adoption of IFRSs could not guarantee improvement in the quality of corporate financial reporting (ROSC, 2002). The CMA annual report of 2002 and the ROSC (2004) notice that there are gaps between authorized accounting standards and actual practices (CMA, 2002; ROSC, 2004). However, the CMA has not put into effect any initiatives to investigate the reasons behind this gap. This study intends to fill this gap by exploring the potential factors that may lead to non-compliance with the EASs and the low presentation of voluntary disclosure in corporate annual report.

Due to the problems of accounting education and practice discussed above, few studies have examined their impact on accounting disclosure. Tai, Au-Yeung, Kwok, and Lau (1990) investigate the reasons for non-compliance with mandatory disclosure requirements in Hong Kong. Results highlighted the following reasons as a cause for non-compliance: difficulties in interpretation of accounting and auditing standards; lack of sufficient accounting knowledge and financial resources to cope with changes in disclosure requirements, shortage of professional accounting staff; and impression management to improve a company's financial position and performance appearance.

Edwards and Smith (1996) aim to investigate preparers' perceptions regarding the costs related to compliance with segment reporting in UK companies. They indicate that competitive disadvantages, confidentiality and low benefits to external users are the main reasons for non-disclosure of segment reporting. With respect to competitive disadvantage, the result indicates that about 33% of the respondents consider competitive disadvantage a main concern. In addition, the administrative costs of collecting and processing data are not, generally, a reason for non-presentation of segment reporting since about 10% of the respondents indicate that their information systems require significant changes to be able to produce segment information.

Al-Mulhem (2003) investigates the obstacles for non-compliance with mandatory disclosure requirements in Saudi companies. The study aims to identify preparers and external auditors' perceptions for causes of non-compliance through a questionnaire survey. The results point to the weakness of enforcement mechanisms and accounting education programs, the lack of qualified accountants, lack of awareness regarding accounting concepts and objectives of financial reporting, difficulties in understanding and interpreting disclosure requirements and lack of sufficient financial resources for accounting training as the main reasons for non-compliance with mandatory disclosure requirements.

3. Accounting education in Egypt

Accounting education has been present in Egypt since 1837 through the establishment of the School of Accountancy but it was closed in the late 1840s. Then, in 1868, the School of Survey and Accountancy was established. Accounting education became present as an organized institution in 1911 with the establishment of the Higher School of Commerce, which became the faculty of commerce in the Egyptian University (Cairo University now). Currently, 27 government and 24 private universities, besides a large number of higher institutes, offer various degrees in accounting including Bachelor, Diploma, Master and PhD. Undergraduate study in accounting consists of 4 years of study for a B.Com with a major in accounting. The courses cover a large list overlapping courses. However, there is no course that covers professional ethics and the interpretation and implementation of the EASs/IFRSs. Kayed (1990) highlights some problems in accounting education in Egypt as the following:

- Lack of updated textbooks in Arabic and a shortage of discussing topics such as the role of accounting in economic development and research methodology.
- Very little attention has been given to practice problems. Textbooks mainly focused on technical rather than conceptual issues.
- Free government education and over-population create heavy demand on higher education which, in turn, is given limited financial and technical resources.
- Consequently, Egyptian universities suffer from a very poor staff/students ratio and a busy schedule of faculty members.
- Inadequacy of libraries and other educational materials.

In addition, ROSC (2002) indicates that the accounting curricula cover only basic topics and fail to present international standards and practice and suffer from the shortage of implementation guidelines on the EASs/IFRSs. Such problems threaten the quality of accounting education in government universities. All these problems in Egyptian accounting education have been reflected in accounting practice. Accounting education problems result in a lack of accounting knowledge of most graduates, lack of knowledge regarding the application of accounting and auditing standards, outdated Arabic translations of the IFRSs and the precedence of tax accounting over financial reporting. It is not surprising that auditors and clients decide on and prepare together accounting treatments and disclosures in financial reports (ROSC, 2002). Kayed (1990) argues that the development of accounting education in Egypt requires incorporating a case study approach, field trips, practical training and real world problems in accounting education.

4. Research design

4.1. Primary data collection method

Based on prior studies regarding the factors that impede the presentation of mandatory and voluntary disclosure, this research aims to generate inductively themes regarding the factors that the interviewees mentioned in their responses. This section presents the main features of a semi-structured interview as a method for collecting primary data. It also discusses the process of interviewing, the credibility and dependability of qualitative interviewing and interviewees' selection process.

In a semi-structured interview, an interviewer has a series of themes and questions to be explored during the course of the interview. The order of the themes and questions may vary from one interview to another; also the interviewer has the chance to add or remove questions depending on interview context (Bryman & Bell, 2012, chap. 4; Saunders, Lewis, & Thornhill, 2007, chap. 10).

Inductive and deductive approaches have been used to identify the categories/themes used in qualitative data analysis. Thus, the semi-structured interview is a suitable research method for this study because it helps in identifying the factors that hinder the presentation of mandatory and voluntary reporting. The semi-structured interview assists in exploring certain topics in more depth and providing substance and texture to the topic under examination by adding illustrative evidence to the quantitative results (Corbetta, 2003, chap. 10). It provides a flexible method that can be utilized in different empirical situations and shaped according to the context of the interview itself so that the interviewer is able to react to themes that emerge during the course of interview (Corbetta, 2003, chap. 10; Legard, Keegan, & Ward, 2003).

4.2. The process of interviewing

This study began the interview by introducing the research objectives, importance and ethical considerations. The main aim of this introduction is to establish a well-balanced rapport and to remove any misunderstanding regarding the meaning and purpose of the research especially where the tradition of research is not well-established (Hatem, 1994). In addition, the researchers use the interview guide to control the course of the interview without overlooking the importance of probing questions. Finally, in respect of interview recording, similar to Kamel (2006) and Hassan (2008), the researchers were not allowed to record the interviews. Therefore, notes were recorded mainly during and immediately after the course of each interview.

4.3. Interviewees selection process

The sample was collected based on certain criteria in order to yield a sample that is theoretically and empirically meaningful (Mason, 2002, chap. 4) and therefore the knowledge and experience of interviewees are necessary criteria in selection process in order to obtain more in-depth insights regarding research questions (Remenyi, Williams, Money, & Swartz, 1998, chap. 8). In line with these conditions, the interviewees in this study are selected on the following criteria:

- They should have the required and the essential knowledge and experience in the field of financial reporting and accounting standards.
- They are willing and enthusiastic to be interviewed.

In this study, the participants are academics, external auditors, financial managers besides the CMA, the EGX and EIoD disclosure department officers. One of the researchers contacted staff from three leading Egyptian universities who are interested and experienced in financial reporting. In addition, the researchers interviewed six accountants in auditing firms that are affiliated with international auditing firms. The researchers sought the help of these firms to arrange interviews or provide contact details for managers in their client companies who satisfy the interviewing criteria. After several attempts, two financial managers agreed to be interviewed. Finally, the researchers contacted the CMA, the EGX and the EIoD requesting an

Table 1 – Interviewee description.

Interviewees	Interviewee Code	Position	Qualification	Years of experience
Academics	AC1	Lecturer	PhD	12
	AC2	Assistant Professor	PhD	17
	AC3	Professor	PhD	29
External Auditors	AD1	Audit manager	Diploma in auditing and financial accounting	14
	AD2	Audit manager	Diploma in auditing and financial accounting	11
	AD3	Vice partner	Diploma in auditing and financial accounting	21
	AD4	Executive manager	Diploma in Tax, auditing and financial accounting	16
	AD5	Audit manager	Diploma in auditing and financial accounting	16
	AD6	Partner	PhD	35
Regulators	RG1	Vice manager	Diploma in financial accounting	15
	RG2	Vice manager	MBA	9
	RG3	Manager	Diploma in financial accounting	25
	RG4	Manager	MBA	20
Financial Managers	FM1	Manager	Master in accounting and finance	17

interview with managers in their disclosure departments. After several attempts, they allowed the researchers to interview four of their officers. In total, 15 interviews were conducted. The qualification and experience of each interviewee is presented as follows (see [Table 1](#)):

5. Factors influencing IFRSs disclosure: key findings

This section explores the factors that influence the presentation of mandatory and voluntary reporting. To organize our findings related to the factors that influence presentation of mandatory and voluntary reporting we propose the following three category groups. Each category of factors is discussed in some details as follows:

- Factors related to accounting education.
- Factors related to accounting practice.
- Factors related to cost of disclosure.

5.1. Factors related to accounting education

Based on prior literature, four factors have been recognized as a potential threat to reporting practices of Egyptian companies. The potential impact of these factors on mandatory and voluntary reporting is explained as follows:

5.1.1. Inadequate accounting education of managers and decision-makers

According to a regulator (RG-1), due to the lack of adequate accounting education, managers consider preparing financial statements a routine process to satisfy regulation requirements only. Therefore, there is no need to provide more voluntary disclosure. Moreover, an external auditor (AD-4) thought that managers consider compliance with the EASs an optional decision and the standards could be applied in a selective manner. [Tai et al. \(1990\)](#) and [Al-Mulhem \(2003\)](#) indicate that managers, especially in developing countries, suffer from difficulties in understanding the requirements of company law and accounting standards. In addition, [Akathaporn et al. \(1993\)](#) argue that managers of Thai companies, especially small and medium sized ones, have very little knowledge about the role and benefits of financial reporting.

The inadequate accounting education of managers and decision makers impaired the importance of compliance with accounting standards and voluntary reporting. A regulator (RG-2) believed that information such as risk disclosure might not be included in financial reports due to the lack of managers' knowledge regarding the importance of accounting disclosure. An academic (AC-1) remarked:

The inadequate accounting background of managers and decision makers may lead to the failure to recognize the important role of mandatory and voluntary risk reporting in supporting the company's image.

In the same vein, an external auditor (AD-5) added that managers' accounting knowledge is very poor and therefore they believe that adherence to accounting standards or presentation of voluntary reporting, including risk reporting, is useless. Several participants highlighted that the inadequate accounting education of managers and decision-makers is an obstacle to the development of the financial reporting practices of Egyptian companies since they resist any attempt to enhance accounting practices including risk reporting. An external auditor (AD-3) remarked:

Managers' knowledge concerning financial reporting is very poor and hence they opposed the presentation of voluntary risk reporting within financial reports. In several cases, we put pressure on the managers to accept the compliance with risk-related EASs.

Similarly, a financial manager (FM-1) indicated that he faced strong confrontation from top management when he proposed some enhancement in the financial reports and related disclosure such as segment reporting. In the same vein, a regulator (RG-2) highlighted that any attempt from the regulatory authorities to develop financial reporting and disclosure practices of Egyptian companies receive very low acceptance from companies. An external auditor (AD-1) commented that the main problem in the application of EASs is low management awareness concerning the necessity to keep pace with the changes that have occurred in accounting standards and practices. A regulator (RG-1) pointed out that the problem of inadequate accounting education for managers and decision-makers is exaggerated in small companies because managers in these companies may suffer from a shortage of accounting knowledge and do not appreciate the role of financial reporting in supporting the market value of companies' shares.

On the other hand, one of the interviewees (FM-2) argued that managers' lack of accounting background does not mean that the company will not prepare proper financial statements because the external auditor will assist in preparing financial statements through highlighting what the company should report.

5.1.2. *Bookkeeping and procedures-oriented accounting education*

Regarding the impact of the emphasis on bookkeeping and reporting procedures, all the interviewees argued that accounting education limits the attention to a procedures-approach to accounting and pays less attention to financial reporting which in turn may impede presentation of mandatory and voluntary reporting in the annual reports of Egyptian companies. This result is in line with the conclusion of [AAA \(1976\)](#) that significant focus on bookkeeping and accounting procedures is a major feature of accounting education in developing countries. An external auditor (AD-3) remarked:

Accounting education does not discuss accounting disclosure properly. Students in accounting sections do not know the real meaning of the word 'Disclosure'. Therefore, it is difficult for them to deal with accounting disclosure-related standards especially those related to highly sensitive topics such as risk reporting.

Moreover, a financial manager (FM-1) indicated that accounting education does not provide illustrations and case studies on how to report certain information such as segment reporting.

The participants identify three main characteristics of accounting education in Egypt that contribute to low presentation of mandatory and voluntary reporting. First, an academic (AC-3) argued that accounting education pays less attention to the application of financial reporting standards and this, without doubt, will lead to a limited accounting knowledge of the graduate. Second, an external auditor (AD-5) believed that there is no clear approach regarding how to train students on the application of financial reporting standards. It is very rare to find a graduate able to deal with the standards and who is aware of the importance of complying with them. Third, accounting education focuses mainly on accounting measurements and ignores accounting disclosure, which in turn distorts the accounting knowledge of a graduate. An external auditor (AD-6) indicated that accounting measurement dominates the accounting curricula in Egyptian universities. It is worth mentioning that a regulator (RG-4) indicated that in an interview of 65 candidates, he found that most candidates did not have sufficient knowledge about accounting disclosure and financial reporting standards. Only three candidates were able to discuss and present a reasonable understanding regarding accounting standards requirements and financial reporting.

5.1.3. *Limited emphasis on the conceptual framework and the objectives of financial reporting*

[Lin and Deng \(1992\)](#) highlight the importance of the objectives of financial reporting, qualitative characteristics of accounting information and basic elements of financial reporting in forming a well-established framework for accounting education and practice. Regarding the impact of limited emphasis on the conceptual framework and objectives of financial reporting on reporting practices, all the interviewees indicated that a relatively low importance has been given by accounting education to the conceptual framework and objectives of financial reporting and this is a main reason for low presentation of mandatory and voluntary reporting. [Kayed \(1990\)](#) indicates that Egyptian accounting education focuses principally on technical rather than conceptual issues. Moreover, [Al-Mulhem \(2003\)](#) points out that lack of awareness regarding the objectives of financial reporting is a key reason for non-compliance with disclosure requirements in Saudi companies. An academic (AC-2) remarked:

This is an important factor for non-compliance with accounting standards and low presentation of voluntary disclosure in the annual reports of Egyptian companies. The relative weight of accounting measurement in the curricula is much larger than the relative weight of accounting disclosure. This in turn led the accountants to focus mainly on accounting measurement and ignore disclosure in annual reports.

This result is consistent with the finding of [Samaha and Stapleton \(2008\)](#) that Egyptian companies tend to comply more with accounting standards related to measurement aspects than accounting standards related to disclosure aspects. [Street and Gray \(2002\)](#) and [Al-Shammari, Brown, and Tarca \(2008\)](#) reach a similar conclusion. They find that compliance with disclosure requirements is lower than compliance with measurement requirements. Moreover, a low emphasis on the conceptual framework

results in a distortion of students' knowledge regarding their importance as guidance to accounting practices. A regulator (RG-3) indicated:

Accounting education does not pay significant attention to the conceptual framework for the preparation and presentation of financial statements in spite of its importance in highlighting the role of accounting disclosure which in turn influences accountants' awareness regarding the importance of compliance with accounting standards and presentation of voluntary disclosure including risk reporting.

An external auditor (AD-1) pointed out the failure to present accounting disclosures that satisfy the qualitative characteristics of accounting information as a consequence of limited emphasis on the conceptual framework. A regulator (RG-2) supported this point of view by stating that accountants do not know how to prepare disclosure in accordance with qualitative characteristics of accounting information. Interestingly, an external auditor (AD-6) added that several accountants and auditors are confused concerning the basic concepts of accounting. He stated:

I discovered that a large number of practitioners do not understand the difference between the assumptions, principles, constraints and qualitative characteristics of information. They do not know the difference between these elements because of the neglect of introducing the Conceptual Framework in accounting education. Certainly, this will influence disclosure practices.

It is worth mentioning that a regulator (RG-2) indicated that to encourage companies to apply corporate governance principles, EIoD held a competition between the top 30 listed companies for the best website and annual report. The results were disappointing because several companies have only financial statements and have no idea about the annual reports.

5.1.4. Lack of sufficient practical training of accounting students

Tipgos (1987), Kayed (1990), Akathaporn et al. (1993) and Al-Basteki (2000) highlight the importance of practical training or internship programs for accounting students during their undergraduate education as a key factor to enhance accounting practice. This kind of training will assist them in applying the accounting knowledge they gain in real world situations (Lin & Deng, 1992). Regarding the impact of practical training of undergraduate students on disclosure practices, all the interviewees agreed that the lack of relevant practical training of students has a negative impact on risk reporting practices of Egyptian companies. The absence of practical training leads to shortage in graduates' accounting knowledge which in turn undermines the importance of accounting disclosure. An academic (AC-3) emphasized that:

Students in accounting sections do not get any training regarding accounting standards. Therefore, the preparation of financial statements in accordance with EASs and the presentation of voluntary disclosure is questionable.

An academic (AC-1) indicated that the absence of practical training limits graduates' accounting knowledge to procedural aspects only and hinders the application of accounting standards in practice. An external auditor (AD-5) added that the students do not receive any practical training which can contribute to building their accounting skills and knowledge. Consequently, the result is limited disclosures. Moreover, an external auditor (AD-2) highlighted that the absence of relevant practical training as one main reason for non-compliance with accounting standards because students do not practice how to apply them in preparing financial statements. A regulator (RG-3) remarked:

The lack of practical training for students leads to low knowledge about the process of preparing financial reports, and low awareness regarding the role of accounting standards in this process and the merits of voluntary disclosure.

Another external auditor (AD-1) highlighted the fact that the absence of practical training is a major reason that students have no idea about best voluntary disclosure practices. Participants identify a number of reasons that hinder the provision of practical training to graduates of accounting sections in Egyptian universities. First, the large number of students accepted by business schools has been given as a major reason for the absence of practical training to students (AC-2 & RG-4). Second, an academic (AC-3) pointed out that funding problems and lack of companies' awareness toward the importance of their contribution in students' training are key obstacles to offering practical training to undergraduate students.

5.2. Factors related to accounting practice

Based on previous studies, five problems related to accounting practice in Egypt have been identified as potential obstacles to mandatory and voluntary risk reporting in the annual reports of Egyptian companies. Interviewees were asked to explain their views regarding the potential impact of these factors on risk reporting practices.

5.2.1. Lack of qualified accountants

The shortage of experienced accountants is one of the main obstacles to the adequate implementation of accounting standards (UNCTAD, 2008). Interviewees argued that the lack of qualified accountants has a significant negative impact on compliance levels with the EASs as well as voluntary presentation of risk information. This result is consistent with AAA (1976), Tai et al. (1990) and Al-Mulhem (2003) who agree that a shortage of competent accounting staff is a key reason for noncompliance with disclosure requirements. A regulator (RG-1) commented:

Yes, there is a significant shortage of qualified financial accountants in many companies, which negatively affects the quality of financial reports.

This shortage of qualified financial accountants has significant negative consequences on risk reporting practices. An academic (AC-3) stated:

The significant shortage in qualified accountants results in a divergence in Egyptian companies' accounting practices as benchmarked against EASs and IFRSs.

Interviewees presented two key reasons for a shortage of qualified financial accountants in Egyptian companies. First, interviewees from the academic group (AC-1) and the external auditors group (AD-1 & AD-2) highlighted the lack of up-to-date accounting knowledge as a major reason for the shortage of qualified accountants. An academic (AC-1) stated:

Most - a large proportion - of the accountants in Egyptian companies do not up-date their knowledge about accounting standards and their amendments, particularly those related to disclosure requirements. This lack of knowledge negatively influences the quality of financial reports particularly the disclosure of risk information.

In the same vein, an external auditor (AD-1) remarked:

From my experience, 90% of the accountants in Egyptian companies do not have sufficient experience in the preparation of financial statements to make them consistent with EASs and IFRSs and many of them even do not read the EASs.

Second, participants from the academic group (AC-5 & AC-3) and the external auditors group (AD-3 & AD-4) highlighted a lack of sufficient training as a potential reason for lack of qualified accountants. An external auditor (AD-3) indicated that:

Most accountants have the minimum level of accounting knowledge and suffer from a lack of practical training, which in turn influences their abilities to prepare financial statements and disclosures in accordance with the Egyptian Accounting Standards. They need more courses to gain experience and enhance their accounting knowledge.

This result is consistent with Dahawy et al. (2002) who argue that immediate adoption of the IFRSs does not allow sufficient time for companies and the accounting profession to prepare. Preparers, users, regulators, professional agencies and educators should be engaged in the planning and implementation of IFRSs (UNCTAD, 2008).

5.2.2. Adequacy of IFRSs to Egyptian environment

Interviewees argued that the application of IFRSs is adequate for Egypt. The main reason for this point of view is the important role of IFRSs in attracting more foreign investments to the Egyptian economy especially after the adoption of the privatization and economic reform program in the early 1990s. An external auditor (AD-2) remarked:

Given the economic reform program adopted by the Egyptian government in the 1990's and in line with the objective of attracting foreign investments, it is essential to apply IFRSs. Many foreign companies have branches in Egypt and hence there is a need for the application of international standards when preparing financial statements.

A financial manager (FM-1) argued that the IFRSs are designed to fit all countries. Egypt has become a magnet for foreign investments and thus the application of EASs that are based on the IFRSs has become a necessity. In the same vein, an academic (AC-1) added:

There is a trend for the application of IFRSs in the international arena and not keeping pace with this trend will make accounting practices in Egypt lag behind those practices internationally accepted.

Alternatively, four of the interviewees argued that the IFRSs are not adequate for the Egyptian environment. Consequently, Egyptian companies may depart from full compliance with these standards. They mention three main reasons for the inadequacy of

IFRSs. First, there is a need to harmonize the EASs with current accounting practice to make sure that they are suitable for the Egyptian environment and gain wide acceptance from practitioners. An academic (AC-3) stated:

The application of the IFRSs has occurred without any reconciliation to the very nature of the Egyptian environment. EASs are merely a translation of IFRSs without any attempt at harmonization.

Second, a number of accounting standards apply accounting treatments that are unknown to the preparers of financial statements, which in turn lead to non-compliance. An external auditor (AD-6) expressed the following opinion:

Several accounting standards such as financial instruments use unfamiliar accounting treatments to existing accounting practices in Egypt. They are not being taught to students at undergraduate/postgraduate level in the university.

Third, a financial manager (FM-2) believed that business transactions in Egypt, in terms of complexity, are completely different from those in the international arena. Therefore, it is not appropriate to apply the IFRSs in the Egyptian context.

5.2.3. Lack of effective accounting and auditing profession

Successful implementation of the IFRSs requires extensive and ongoing support from the accounting profession in building the technical capacity of its members (UNCTAD, 2008). The accounting profession in developing countries is very weak and based on an outdated institutional framework. Therefore, there is a need to establish an effective professional agency that could monitor and regulate the profession (Al-Basteki, 2000). Regarding the impact of the accounting profession on the risk reporting practices of Egyptian companies, all the interviewees indicated that a lack of an effective accounting profession led to a low compliance with mandatory risk reporting and low presentation of voluntary risk reporting in the annual reports of Egyptian companies. A regulator (RG-4) highlighted the impact of a powerless accounting profession on accounting practices:

The accounting and auditing profession is very weak and does not exercise an effective role in training its members on the application of EASs or in developing their professional skills. Moreover, the profession does not provide relevant continuing education programs for its members. In addition, the profession lacks powerful punishment mechanisms to oversee the professional performance of accountants and auditors.

Consequently, accountants in Egyptian companies have become less concerned about applying accounting standards in preparing financial statements. A financial manager (FM-1) expressed the following opinion:

The accountants' key objective is to prepare financial statements that match management's point of view in order to ensure its approval even at the expense of compliance with accounting standards especially since there are no strict sanctions for non-compliance with accounting standards.

The interviewees advanced several reasons for the weak status of the accounting and auditing profession in Egypt. A number of interviewees believed that the main reason for such a weak profession is the law. Accounting and auditing practices in Egypt are organized by law 133/1951 and its amendments. This law is outdated and has not kept pace with structural changes in the Egyptian economy. Moreover, the law does not include any strict rules regarding continuing education. Besides, the law's administrative sanctions are not effectively applied and the legal liabilities of accountants and auditors are vague. An academic (AC-3) argued that the legislation that organizes the profession is obsolete, does not require the application of IFRSs/EASs and does not support the legal and professional accountability of accountants and auditors. Moreover, another external auditor (AD-6) highlighted the powerlessness of the law by stating:

The law, which governs the profession, is very outdated and free from strict sanctions for the violation of accounting standards. Consequently, accountants have become indifferent to preparing the financial statements in accordance with the requirements of accounting standards.

Kothari (2001) indicates that shareholder litigation against auditors is infrequent in developing countries. ROSC (2002) asserts that this is the case in Egypt. An external auditor (AD-6) commented:

Apart from the CMA auditors' registry, the monitoring of audit quality is absent. There is no control over the performance of auditors or assessment for their competence in performing the duties entrusted to them in accordance with auditing standards.

Several interviewees indicated that the accounting and auditing profession in Egypt is weak because professional bodies that organize and regulate the profession do not perform their role in developing and improving accounting practices as anticipated. An academic (AC-2) remarked:

Agencies overseeing the accounting profession lack efficiency in training the accountants/auditors and providing them with the essential skills required for the application of accounting standards.

5.2.4. *The lack of an effective enforcement mechanism*

An enforcement mechanism is a key element in the effective application of accounting standards because the benefits of a set of financial reporting standards are conditional on consistent enforcement of the standards (UNCTAD, 2008). Regarding the impact of the absence of an effective enforcement mechanism on mandatory and voluntary risk reporting, 13 of the interviewees argued that the lack of an effective enforcement mechanism is a main hindrance to compliance with mandatory and presentation of voluntary risk reporting. This result is consistent with that found in the Saudi context (Al-Mulhem, 2003). Al-Shammari et al. (2008) reveal a similar conclusion for Gulf Cooperation Council Member States. This confirms Saudagaran and Diga's (1997) point of view that enforcement is a major concern in developing countries. The weak enforcement mechanism enables companies to violate accounting standards (Kothari, 2001). Taplin, Tower, and Hancock (2002, p. 175) highlighted that the lack of effective enforcement the "production of accounting rules will be nothing more than symbolic behavior unless it is accompanied by some program for monitoring compliance with those standards, and for imposing sanctions for non-compliance.". The existence of an effective mechanism to supervise the application of accounting standards is a necessity (Dao, 2005).

A number of interviewees indicated that although the Capital Market Law and listing and delisting rules of the EGX include several administrative sanctions and fines, the application of these sanctions on companies that violate the rules is ineffective. In addition, the penalties are not strictly enforced and do not lead companies to comply with accounting standards. An academic (AC-2) expressed the following opinion:

Despite the existence of administrative measures and fines applied by the CMA and the EGX on companies that do not comply with accounting standards and listing rules, their implementation is not effective. For example, a company may be delisted from the Egyptian exchange for reasons other than non-compliance with accounting standards.

In the same vein, a regulator (RG-1) remarked:

Non-strict fines do not have significant impact on companies. The fine for a delay in submitting financial reports is L.E. 5000 and there are no strict fines on non-compliance with disclosure requirements of EASs and listing/de-listing rules of the EGX.

Moreover, an academic (AC-2) indicated the attention of the CMA is limited to format aspects only and insufficient attention has been given to the content of annual reports. El-Essely (2005) and Abd-Elmalek (2006) came to the same conclusion. Furthermore, the lack of criminal commitments for the violation of accounting standards and listing rules weakens compliance with them. A regulator (RG-3) highlighted this:

Although there are several measures to force listed companies to comply with the disclosure requirements, the violation of these requirements has no criminal liabilities. The punishment is limited to blame only without any strict actions. If a company did not comply, there is no action against it. Currently, it is very difficult to write-off a company because of non-compliance with disclosure requirements.

This point of view confirms Akathaporn et al. (1993) and ROSC (2002) who conclude that accounting standards are frequently breached because their violation is not considered a criminal or civil violation. The UNCTAD (2008) argues that the application of the IFRSs lacks the necessary legal backing. In addition, the EFSA and the EGX do not attempt to provide any motivations to listed companies for the presentation of voluntary risk disclosure or to highlight the well-presented risk disclosure reported in some Egyptian companies' annual reports in order to encourage other companies to follow the path of these companies. An academic (AC-1) remarked:

It is very important to present incentives for voluntary risk disclosure such as a reduction in annual subscription fees of the Egyptian exchange or highlighting the names of companies that present distinctive risk disclosures.

5.3. *Inadequate continuing education*

Continuing education is an important element in the development of accounting practice in developing countries because it ensures that qualified and competent accountants enter the profession and provides the chance to update their accounting knowledge and skills to cope with a rapidly changing business environment (Al-Basteki, 2000; Tipgos, 1987). In addition, Jensen and Arrington (1983) highlight the need for overseeing not only the form but also the content of continuing education programs by regulatory agencies. All the interviewees indicated that this has a negative impact on mandatory and voluntary risk reporting. Because of the lack of continuing education, auditors do not perform their tasks effectively and fail to establish appropriate professional judgements about clients' compliance with the EASs. The lack of continuing education contributes to auditors' lack of knowledge about the application of auditing/accounting standards. An academic (AC-1) expressed the following opinion:

Due to the lack of adequate continuing education, several auditors do not update their accounting skills and knowledge. Therefore, they do not know the latest amendments in accounting disclosure related standards and cannot assess the extent to which the disclosure in the client's financial statements is in accordance with accounting standards requirements.

This result confirms the finding of [ROSC \(2002\)](#) that the lack of adequate professional continuing education increases the knowledge gap of external auditors in Egypt. The lack of continuing education is a serious problem for auditors in small audit firms. An external auditor (AD-3) indicated:

This problem is very visible in small audit firms but big audit firms or audit firms with international affiliations are keen to train their staff continuously and force them to complete a certain number of training hours each year as a prerequisite for working in the firm.

Moreover, one of the interviewees (AD-5) highlighted the role of the ESAA in preparing and enforcing general rules of continuing professional training for its members. However, another external auditor (AD-6) criticized the effort of the ESAA in continuing education because of the weak education leaflets and periodicals provided. He stated:

There is a significant lack of well-established continuing education programs provided by the ESAA. Their bulletins and studies are very weak and written by unqualified members who do not follow the scientific approach in writing.

The current effort in continuing education is limited to the members of the ESAA. Therefore, there is a need for an authority that provides continuing education for all the practitioners of the accounting and auditing profession.

5.4. Factors related to cost of disclosure

This subsection aims to identify the impact of disclosure cost, proprietary and non-proprietary cost, on mandatory and voluntary risk reporting in the annual reports of Egyptian companies.

5.4.1. Competitive disadvantages

Accounting researchers employ proprietary cost perspective to explain why managers may withhold information. Interviewees indicated that competitive disadvantages have a negative impact on risk reporting. Egyptian companies may present a low level of compliance with and presentation of mandatory and voluntary risk reporting if this disclosure threatens their competitive advantages. An academic (AC-1) argued that this belief dominates the thought of companies' managements in Egypt. In the same vein, [Dahawy et al. \(2002\)](#) report that managers in Egyptian companies perceive disclosure as equivalent to revealing companies' secrets. Competitive disadvantage has been recognized as a main reason for segment reporting non-disclosure ([Edwards & Smith, 1996](#)). Confirming this point of view, an external auditor (AD-2) indicated that a large number of Egyptian companies avoid complying with the segment reporting standard because of the fear of revealing important strategic information about their business and geographic segments to competitors. A financial manager remarked (FM-1):

Our main belief is if you disclose all the information you have the competitors may read your ideas. Consequently, companies tend to present very limited disclosure. Companies present a minimum level of mandatory risk reporting and refrain from presenting voluntary risk disclosure.

Similarly, another financial manager (FM-2) stressed:

Our company tends to distinguish itself from the competitors. Therefore, we never ever disclose any information we think might worsen our competitive advantage.

This result is consistent with the result reported in the previous chapter that indicates a significant positive association between barriers to entry and mandatory and voluntary risk reporting. Moreover, [Linsley, Shrives, and Crumpton \(2006\)](#) argue that risk information is commercially sensitive information that is related to a high level of competition disadvantages; therefore, managers are reluctant to disclose it.

An academic (AC-1) suggested that the EFSA should work to raise companies' awareness regarding the importance of compliance with and presentation of mandatory and voluntary risk reporting because of their significant impact on investors' confidence in companies' financial reports and cost of capital.

Alternatively, three of the interviewees believed that there is no significant impact for competitive disadvantage on the risk reporting practices of Egyptian companies. They advanced two main reasons for their point of view. First, it is important for a company to report certain information such as segment reporting to support its competitive advantage.

Second, a regulator (RG-1) thought that non-compliance with risk-related accounting standards is more closely related to the lack of effective enforcement mechanism rather than competitive disadvantages.

5.4.2. Cost of collecting, processing and disseminating information or the cost of developing accounting information systems

Interviewees argued that there is no significant impact for non-proprietary cost of disclosure on risk reporting practices. This result is consistent with [Edwards and Smith \(1996\)](#) who indicate that most information systems of British companies did not need significant changes to generate segment information. The interviewees advanced a number of reasons to support their point of view. First, an academic (AC-1) believed that, regardless of the cost, modern accounting information systems have become an

urgent necessity not only for high quality disclosure but also because continuity in the markets requires a very sophisticated information system. Second, another academic (AC-2) argued that due to high technology in the field of information systems the cost of collecting, processing and disseminating information has become relatively low. Third, an academic (AC-3) argued that the management's willingness rather than disclosure cost is the determinative factor regarding the decision to utilize a sophisticated information system to provide relevant risk information. Fourth, an external auditor (AD-6) indicated that presentation of mandatory and voluntary disclosure depends on management's willingness to report accounting information produced by accounting information systems.

Alternatively, six of the interviewees indicated that the cost of disclosure has a negative impact on risk reporting practices. An external auditor (AD-1) argued that the cost of sophisticated information systems is too high which in turn may hinder the presentation of mandatory and voluntary risk reporting. For example, segment-reporting needs more detailed information and existing information systems in several Egyptian companies cannot provide such information. Therefore, according to a regulator (RG-3), high disclosure cost may lead to non-compliance with accounting standards. However, another regulator (RG-4) believed that the problem of disclosure cost is more apparent in small companies than in large companies due to a lack of financial resources.

6. Conclusion

This study aimed to identify the factors that influence the presentation of risk reporting. We found that these factors could lead to low compliance with mandatory and presentation of voluntary risk reporting. Several interrelated and interdependent factors related to accounting education and practice problems that may influence risk reporting practices of Egyptian companies will be summarized in this section to show a low presentation of risk reporting in the annual reports of Egyptian companies.

These factors have been categorized into three groups:

1. Factors related to accounting education (group 1).
2. Factors related to accounting practice (group 2).
3. Factors related to cost of disclosure (group 3).

With respect to group 1, findings indicate that there is an agreement that bookkeeping and procedures-oriented accounting education impaired the importance of accounting disclosure in general and risk reporting in particular. The focus on bookkeeping and accounting procedures limits graduates' accounting knowledge regarding accounting disclosure, which in turn results in low presentation of mandatory and voluntary risk reporting. In addition, Egyptian accounting education pays much more attention to accounting measurement compared to accounting disclosure, which in turn results in inadequate risk disclosure in the annual reports of Egyptian companies. Also, insufficient practical training of undergraduates impaired their ability to apply accounting standards and resulted in low awareness regarding best voluntary disclosure practices. Finally, inadequate accounting education of managers has a significant negative impact on the risk reporting practices of Egyptian companies. Due to an inadequate accounting background, managers think that preparation of annual reports is a routine process and accounting standards could be applied selectively.

With respect to group 2, the results indicated that there is a consensus that the insufficient role of the profession—in terms of monitoring the professional performance of auditors and enhancing accounting skills and knowledge of its members—limits reporting practices of Egyptian companies. The lack of adequate continuing education is a significant reason for low compliance with and presentation of mandatory and voluntary reporting since continuing education is not a requirement for practicing the profession. Moreover, chartered accountants are not able to advise their clients regarding best voluntary disclosure practices including risk reporting. In addition, the lack of qualified accountants results in preparation of financial statements that diverge from accounting standards' requirements. We found that many accountants do not attempt to update their accounting knowledge and do not receive professional training in accounting standards and best voluntary disclosure practices. Finally, the lack of effective enforcement mechanisms hinders compliance with and presentation of mandatory and voluntary disclosure because administrative measures and sanctions are not effectively imposed by regulatory agencies such as the CMA and EGX. There is no attempt to provide incentives to encourage companies to provide voluntary disclosure including risk reporting.

With respect to group 3, findings reveal that the competitive disadvantage is a significant threat to disclosure practices. Egyptian companies refrain from complying with or presenting mandatory and voluntary disclosure because they think that disclosure can reveal sensitive issues and reporting such information may damage their competitive advantage. Also, non-proprietary costs of disclosure, such as the cost of collecting, processing and disseminating information or the cost of developing accounting information systems, has no impact on the reporting practices of Egyptian companies since such costs have become relatively low due to technological enhancement in the field of information systems.

Findings of this study may assist the Egyptian Financial Supervisory Authority (EFSA) to be more informed about the weaknesses in the adoption of IFRSs and guide its efforts to encourage Egyptian companies to comply with the IFRSs. Egyptian companies could gain several benefits from full adherence to the IFRSs such as listing on international stock markets, reducing the cost of capital, the possibility to raise capital internationally and the marketability of their stocks by expanding ownership. Future

research can investigate empirically the impact of the reasons advanced by this research on mandatory disclosure practices in other developing countries.

In terms of international standard setting, the findings of this study assist the IASB to rationalize its efforts and work for supporting professional bodies and accounting education in developing countries, which may reflect in more compliance with IFRSs.

Conflict of interest

There is no conflict of interest.

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