# DETERMINANTS OF COMPLIANCE WITH INTERNATIONAL FINANCIAL REPORTING STANDARDS BY FIRMS LISTED AT THE NAIROBI SECURITIES EXCHANGE

**BY**

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# DECLARATION

This is my original work and has not been presented in any other university or college for examination purpose.

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This research project has been submitted for examination with my approval as university supervisor.

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For others whom I have not mentioned for one way or another, feel appreciated.

Thanks and God bless you all.

# DEDICATION

This project is dedicated to my father, mother, brothers, sisters, grandmother, grandfather, uncle and aunts. I will always remember them as a strong pillar in my life

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# LIST OF ABBREVIATIONS

**FRC** - Financial Reporting Council

**FRRP** - Financial Reporting Review Panel

**GAAPs** - Generally Accepted Accounting Principles

**IAS** - International Accounting Standards

**IASB** - International Accounting Standards Board

**ICPAK** - Institute of Certified Public Accountants of Kenya

**IFRS** - International Financial Reporting Standards

**SMEs** - Small and Medium Enterprises

# ABSTRACT

In the past decades, (IFRS) have gained popularity around the globe as the standard ways of financial reporting. Almost over 150 nations around the world apply IFRS in their presentation of financial information. The question that always arises is, do these firms promptly follow the set standards. The research assessed the determinants **of compliance with IFRS** by firms quoted at NSE using a descriptive research design. The study population composed 64 firms listed at NSE **as at 31 December** 2016 thus the study undertook a census approach. This research collected data **for** five years from 2012 to 2016. The regression method was preferred to analyze as well as determine the effects of each of the independent variables. The results revealed that correlation linking **firm size and** the disclosure index of the firms listed at the NSE was negative and significant but the relationship between profitability and the disclosure index of the listed firms was negative and insignificant. The findings also revealed that the relationship between leverage and the disclosure index of the listed firms was positive and insignificant but the relationship between the disclosure index and age of the firm listed at NSE was positive and significant. The study concluded that the key determinants of **compliance with IFRS by** firms quoted at the Nairobi securities exchange are firm size and firm age. The study recommended that listed firms should ensure that they comply with international financial reporting standards to ensure that their financial reports are relevant, faithfully presented, comparable and understandable.

# CHAPTER ONE: INTRODUCTION

## 1.1 Background of the Study

Financial standards are crucial as they ensure conformity and quality in the reports presented to the public and various stakeholders. According to Katselas and Rosov (2017), financial Reporting standards are a set of guidelines and rules that preparers of financial statements ought to abide by when preparing an entity's accounts. It has protected the accounts as in the past have come under enormous pressure especially from the management when they want to conceal frauds and misrepresentation to the stakeholders. The usefulness of financial reports is confirmed when they can embody the economic realities **and be** presented in a form that can be easily understood (IASB, 2015).

Due to globalization, many organizations are established around the globe resulting to movement of financial reports from one nation to the other. **Carpenter (2001)** carried out a study to establish the correlation linking regulatory efficiency and found that regulating agencies which are mandated with tackling the emerging issues in the profession are capable of dealing with those issues. This study has come under criticism as the agencies are often accused of not able to cope with the constantly emerging issues in the sector.

The need for quality financial reporting can be linked to information asymmetry where managers do not only have access to higher quality but also higher quantity information about business than both the shareholders and debt holders. Agency theory problem thus arise where the management of listed companies is more privileged to access better information about their companies than the shareowners. Information asymmetry and

agency conflict can adversely distort the optimal allocation of resources the capital markets (Katselas & Rosov, 2017). Considering information asymmetry and the agency problem, it became absolutely necessary to put in place a financial reporting system that would require companies to report all material information, financial or otherwise concerning its financial performance (Sun & Rath, 2008).

The contents of financial reports are used as a basis to shape major decisions such as executive compensation, debt covenants, capital raising and making investment decisions. The firm's management due to the advantage they have of accessing the reports many times have altered the reports to give a good representation of the firm's financial position or reports which favor themselves, a practice commonly referred to as earnings management (Sun & Rath, 2008). Che Haat, Rahman and Mahenthiran (2008) stated that the legitimacy of the reports depends on those presenting them which are the firm's directors and top management**.**

### 1.1.1 International Financial Reporting Standards

These are set **standards** which ensure high quality threshold and designed for ease of use in general purpose financial reporting. They were formulated **(FRC)** established in the year **1990** mandated to regulate **standards in the accounts sector.** The committee was formed to improve reporting standards, interpretations and guidelines adopted by IASB meant to encourage professional judgment and provide relief against bogging down with lengthy rules (Ahmed & Courtis, 2005).

The IFRS have set such high standards such that it provides uniformity to people across the world as they use them on daily activities (Ahmed & Courtis, 2005). The uniformity

has been instrumental in increasing transparency in the profession which has in the past been accused of lacking transparency. This has yielded positive when in dire times of funds for various projects as the investors are assured their funds will be used for intended purposes (Alfaraih, 2009). The standards stress that all financial reports should meet all the set standards before it qualifies to be presented to the public (Alfaraih, 2009).

Public as well as private corporate use financial reports for same intention, nevertheless there are areas where users of private company greatly emphasis on the financial reporting. These areas include **liquidity, solvency and cash flow.** The government through the ICPAK has continued to adopt various international reporting standards (ICPAK annual report, 2010).

The quality of the financial reports is determined by the issuance of the reports by the (ISA) under preparation and presentation (Alfaraih, 2009). The reports **quality** depends on many factors **not** the standards alone but the expertise and skills of the preparers hence the need for constant seminars and training which ensure quality of the reports (Agyei-Mensah, 2013).

### 1.1.2 Determinants of Compliance with IFRS

IFRSs are accounting standards which have gained popularity over the past decades across all nations in the world. It's important to examine the level to which organizations conform to these standards. This study will assess firm **size, profitability, leverage and age** at the determinants of compliance with IFRS by listed firms in Kenya.

Firm **size** is among the main variables influencing **firms IFRS compliance** as large firms have image to safeguard **and the** stakeholders hence compliance with these standards is

vital for accountability and compliance. The large firms due to their size enjoy economies of scale hence it's less costly to comply with these standards as compared to small firms (Uyar, Kılıç & Gökçen, 2016). According to Appiah at al. (2016), large firms have a brand name to protect against any bad reputation which may hurt their financial performance**.** Large firms are usually associated with quality level of disclosure (Yiadom & Atsunyo, 2014).

There are numerous literatures on the effect **of firm's financial performance to** their compliance with IFRS. Firms with high turnover are faced with the challenge of public scrutiny from various stakeholders hence the need to ensure they comply with the IFRS (Uyar, Kılıç & Gökçen, 2016). Appiah at al. (2016) posits that theory like signaling theory, revealed that the management of large firms in many times are forced to take advantage of the reporting standards as they want to impress the shareholders as well as the investors who are more interested in the reports. Firms with low turnover on the other hand are complying with the standards in order to explain to the stakeholders the reason behind poor performance (Yiadom & Atsunyo, 2014).

The financing options are the other factor influencing the extent to which a firm will comply with the IFRS. Firms which are highly leveraged are faced with increased costs emanating from agency costs as well as the compliance with IFRS (Uyar, Kılıç & Gökçen, 2016). Firms which are highly leveraged are required to produce high quality reports in order to show their financiers how their funds are being used and the suppliers as well to know whether the firm will be able to honor the money owed (Appiah at al., 2016). According to Yiğit (2014) firms which comply with the IFRS access to the funds from the investors at lower rates as compared to those which don't comply.

The longevity of firms also determines the level of company's disclosed of information. Old firms are associated with financial stability hence don't need to conceal anything from the public. Their employees are more experienced in managing the resources of firms' hence high financial performance in these firms as well as skilled employees to prepare financial reports. Their internal control systems are so advanced such that each and every detail pertaining to the accounting is covered hence disclosure of full information by these firms. Hence, older firms are associated with full disclosure of detailed IFRSs (Demir & Bahadir, 2014).

### 1.1.3 Nairobi Securities Exchange

It **was established in 1954 as** stock exchange before transforming to securities exchange in the year 2011. It is regulated by the Capital Markets Authority (Hamisi, 2012). NSE listed companies are drawn from all economic sectors and are categorized according to industry base. These include agricultural and manufacturing industries, investment, services, Telecommunications, financial and allied among others. In total there were 64 companies listed at NSE (Koros, 2016).

The NSE deals operates in conjunction with other securities markets especially those in the East African region (Koros, 2016). It's the largest securities exchange in East and Central African region. All firms listed at the NSE are mandated to disclose full statements of financial statements for the stakeholders to monitor their funds invested. All the companies in its listed at the NSE are mandatorily required to use IFRS for their financial reports covering the period ended on 31 Dec 1999 and onwards. There is also a set of IFRS that have specifically been designed for the financial reporting by small and medium enterprises (Koros, 2016).

## 1.2 Research Problem

Over the last decades, (IFRS) have become popular around the world. Almost over 150 nations have the use of IFRS in preparation and presentation of their financial statements (Alfaraih, 2009). Generally, IFRS have met some resistance due to the complexity associated with them. This has brought so much trouble to many firms as well as the end users of the statements. The increased complex methods have resulted to high costs particularly to small firms with low turnover (Delloite, 2009).

In Kenya, the auditing industry has experienced huge expansion. The valuation of the industry was over $1.5 billion which was followed by 10% increment in 2012**,** the sector reached a 2 billion mark in the year 2014, and this is large compared to the sectors in developed nations**.** The aiding industry in Kenya has been growing at a tremendous rate. However, due to the exponential growth in the consultancy industry, there has been a growing concern from stakeholders pertaining to the **financial reports from** various auditing firms in the country.

A study by Ouda (2004) identified that public administrator's culture**.** The study also found that established communication channels**;** skilled employees in finance department who can quickly adapt to the change in accounting methods**.** Some scholars have criticized the quality of financial reports particularly under the circumstances where the firm has weak internal control systems (Ball et al., 2003).

Past studies have been conducted on issues, challenges and lessons for IFRS adoption in Kenya. Stainbank (2015) conducted a study on aspects leading to increased IFRS among countries in African continent. The study focused on32 African countries. Hamisi (2012)

in Kenya conducted a study on impact on the implementation of IFRS. The study focused on accounting units in the government ministries in Nairobi County. Both studies present a contextual gap. Moreover, No comprehensive study has been carried on the effect of internal and external factors on compliance with financial reporting standards. The study will therefore seek to answer question; what are the determinants of determinants of compliance with international financial reporting standards by firms listed at the Nairobi securities exchange?

## 1.3 General Objective

To assess the determinants of compliance with international financial reporting standards by firms listed at the Nairobi securities exchange

## 1.4 Value of the Study

The study will have great implication to consultancy firms in Kenya, ICPAK and Academic researchers. The study will aid in policy making by the institute of certified public accountants, which can improve effective implementation of financial reporting standards. This will enhance quality of financial reports, which will be used by stakeholders in making investment decisions.

Consultancy firms will understand the importance of effective implementation of financial reporting standards and the critical role effective implementation plays economic development and investor's decisions. This in return is going to increase their attractiveness to investors and reduce non-compliance costs associated with not filling appropriate tax returns.

The firms listed at the Nairobi Securities Exchange will also understand the challenges consultancy firms face in their quest to meet their tax obligation. This study will help firms listed at the NSE to come up will policies and regulations that will enhance tax compliance on consultancy firms not only in Nairobi but all over the country.

# CHAPTER TWO: LITERATURE REVIEW

## 2.1 Introduction

The topic covers available literature on main variables of the study. It will therefore **present** theoretical review and the empirical review. The chapter further shows the conceptual framework and a summary of the literature.

## 2.2 Theoretical Framework

This section presents provision of the theoretical foundation that this study is based on. Esper, Mentzer and Stank (2008) emphasize that a good research should be grounded on. The private interest theory, theory of corporate financial management and the agency theory were explored as the key theories for the study.

### 2.2.1 Private Interest Theory

According to this theory, regulation is power given on a body to ensure certain standards are met (Stigler, 1971). Interest groups demand for regulation determines the level of control provided. The private sector envisages regulation as means by the government to distribute income across all sectors in the economy.

The regulatory in financial sector is vital to the economy as it ensures financial crisis is avoided at all times through the set efficient systems which ensure quality among all the financial institutions. The regulators have to be kept on toes to ensure the high standards are maintained and promptly followed (Das & Quintyn, 2002). The relevance of this theory is that the IFSR compliance is an important aspect in an effort to bring stability in

financial sector and the whole economy as well. This has to be achieved through ensuring the regulators are free from any political interference.

### 2.2.2 Theory of Corporate Financial Management

One of the theories pertinent to this study is the 'Theory of Corporate Financial Management' which summarizes broad flow of financial literature and the 'Normative Theory'. The normative theory focuses on the procedures used in the presentation of financial statements (Ijiri 1975; W & Z 1986). Ijiri viewed this theory as special one whereby, it starts by setting goals which are then used to get the accounting procedures there from. Thus, a financial regulator may start by setting goals which may vary from the normal accounting practices depending on the situation he or she is facing (Chambers, 1966) on the other hand one may develop the existing practices from the ones (Ijiri, 1975). It's important to note that, not all financial regulators are deductive in identifying the accounting practice (Paton & Littleton, 1940).

Normative accounting theory comes in handy to the corporate world particularly in situation whereby they are faced with challenging decision making situation. Study by Mclnnes and Carleton (1982), reported that the accounting model is not satisfactory especially in situations whereby the institutions are faced with a certain ambiguity in decision making. It is observed that there is a constraint in constructing the information in order to bring clarity on the **normative framework** (Bratteteig & Gregory,1999).

### 2.2.3 Agency Theory

The agency theory originated from Berles and Mean (1932) but was advanced further by Jansen and Meckling (1976). Theory above is anchored on the thought that agency costs related with conflict resolution between owners and agents in a contemporary corporation

is an outcome of distinction of management from ownership (Jensen & Meckling,1976). This theory recognizes agency relationship, that is, the principal/ company, assigns the role to a different member. Agency theory envisages use of corporate governance mechanisms in monitoring and minimizing conflicts in principal - agent relationships in corporate setting (Jensen & Meckling, 1976). The above principle views the presence of diverging interests of the firm's management and shareholders which emanates from split-up shareholders control in contemporary firms (Yiadom & Atsunyo, 2014).

The agency theory **"**the systems whereby the investors ensure their finances which are managed by the agents are safe and secure" (Kamwenji, 2014). Agency theory identifies the dominant poor running of corporate through principal's warrant executives to act in shareholders' interests and their own (Appiah at al., 2016).

Jensen and Meckling (1976) on their study on the conflict between **principals** and agents lead to agency cost. Firms associated with high gearing levels are associated with high Agency costs as more revenues are expected to be transferred to the debtors. These companies are expected to have full disclosure of their financial statements in an attempt of reducing the investors' funds are secure (Yiadom & Atsunyo, 2014).

## 2.4 Empirical Review

Uyar, Kılıç and Gökçen (2016) investigated Turkish firms' compliance of IFRS. It used primary data as the method of collecting data. **The** study found that the firms compliance varied as some were more compliant compared to others. The study further revealed that other factors influencing compliance was the number of foreign directors in the firm's board, employees' expertise as well as the age of the firm.

Appiah at al. (2016) examined the correlation linking 10 firms unique characters to compliance with IFRS in Ghana which covered a five-year period from mid 2000 to year

2012**. It** applied a cross sectional and analytical research design that involved firms listed at securities exchange in Ghana. The study found out strong direct correlation between the two phenomena's. The study revealed that IFRS compliance in the country varied according to the sector they were.

**Yiadom and Atsunyo (2014)** sought to establish the level of compliance of IFRS among firms listed at (GSE)**.** The researcher used a checklist to devise a compliance index to quantify **compliance level.** The study findings revealed that compliance level in the country was averaging 87 percent. The factors such as the firm's age, turnover ratio, employees' expertise, the firm sector were directly correlated to compliance.

Tsegba, Semberfan and Tyokoso (2017) studied impact **of** compliance level among Nigerian firms. Primary data was the preferred method of collecting data. **The** study showed that compliance level was high among the firms with high profitability had strong direct correlation while firms leverage revealed weak direct correlation to firms compliance with IFRS.

Fekete, Matis and Lukács (2008) investigated the level of compliance to IFRS among firms listed at Hungary securities exchange, by identifying factors influencing compliance. The findings revealed that the size of a firm as well as the sector its situated has a positive correlation to the extent at which a firm complies with the IFRS. The study concluded huge firms especially those in tech industry are best compliers of the IFRS as they show firms accountability.

A study by Demir and Bahadir (2014) investigated the extent of firms' **IFRS compliance** among Turkish firms. The study sampled 168 companies listed at turkey securities exchange as at the year 2012. The findings established that the compliance level dependent on the expertise of the auditors who annually audit the company's financial reports. The study further revealed an inverse correlation linking compliance to gearing level. Additionally, the study found no relation linking old firms to high levels of IFRS compliance.

In Kenya, Mutai (2014) examined the impact of IFRS compliance among firms listed at NSE. The population comprised of 61 companies listed at NSE. Primary data through use of questionnaires was the preferred method for data collection which was analyzed using the **regression** model. It was established an existence of direct correlation linking the variables, which meant that a unit rise **in independent variable** resulted into a corresponding increase in the dependent variable.

Outa (2011) in his research to establish **the** role **of IFRS on** reporting **quality of financial** reports in Kenya. The study focused mainly on the accounting standards on release of quality reports to establish how reporting has improved due to the adoption of the IFRS in the country. The researcher used self-developed questionnaires and quantitative analysis in collecting and analyzing data respectively. Results revealed a weak positive correlation linking adoption of IFRS to financial reports improvement.

Koros (2014) examined the improvement of **reportin**g practices among firms listed at NSE following the adoption of IFRS. Data was obtained for 60 companies at NSE over 5 year period obtained from secondary data sources, which included NSE handbook and companies' websites. It was analyzed using mean scores, standard deviation and

correlation matrix and**.** Study findings revealed mean of 3.81611 confirming a marginal improvement compared to 2011 mean (3.7546). The study concluded that adoption of new IFRS, amendments; revisions and improvements do lead to improved **financial reporting** though the improvement was not significant.

Kamwenji (2014) studied how **IFRS** lead to improvement **of accounting** standards among the **SACCOs in Nairobi County.** The **descriptive method which targeted** 34 deposit taking SACCOs **in Nairobi County.** Data was obtained from closed and open-ended questionnaire. The study found out that the adoption of IFRSs, majority of the SACCOs were transparent and honest in disclosure as well as the **presentation of** accounting information was uniform with other institutions which had adopted IFRSs. The study concluded that adoption of IFRSs in the SACCOs had improved disclosures, it had improved the relevance, reliability and understandability of accounting information provided in the financial statements and related disclosures.

Monari (2015) examined the impact of IFRS on Public institutions and how they improve their financial reporting in Kenya. The population of study was public institutions that had adopted accrual based IPSASs. A total of 196 non-commercial public sector institutions were to adopt IPSASs accrual as per the data from Public Sector Accounting Standards Board. The study found out that as a result of adoption of IPSASs by the public sector entities there is improvement in accountability, asset management and transparency on financial reporting in public institutions. Hence this has brought about consistency in financial reporting, enhanced decision making and has improved internal control systems.

## 2.5 Conceptual Framework

A **conceptual framework has been developed revealing the** determinants of **compliance with IFRS by firms quoted at the** NSE**.** The independent variables of the study comprises of firm size, profitability, leverage and firm age while the dependent variables will be compliance with IFRS.

**Independent Variable** **Dependent Variable**

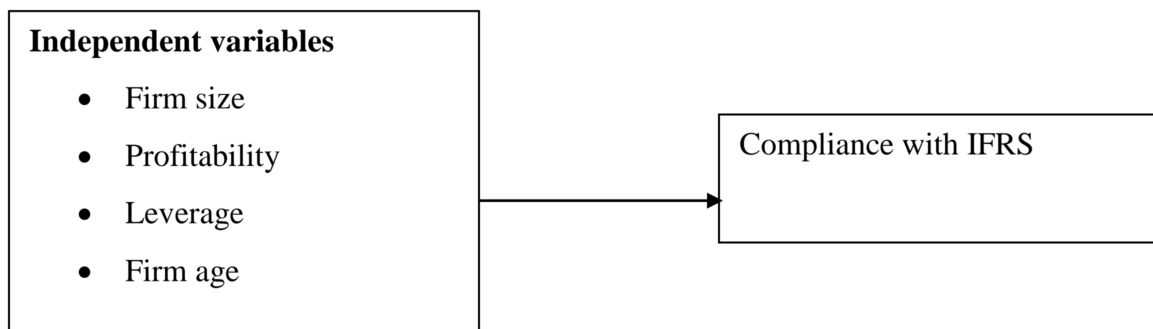


**Figure 2.1 Conceptual Model**

## 2.6 Summary of Literature Review

Mclnnes and Carleton (1982), argues that the accounting model is not satisfactory especially in situations whereby the institutions are faced with a certain ambiguity in decision making. It is observed that there is a constraint in constructing the information in order to bring clarity on the **normative framework.**

Several scholars have done studies on factors affecting the financial reporting standards in Kenya (Hamisi, 2012, Mihret & Yismaw, 2007. Majority of the available literature on the topic under study is carried out in developed nations which opearate and face different challenges to those in Kenya. Hence, the study was conducted so as to fill the identified research gaps.

## CHAPTER THREE: RESEARCH METHODOLOGY

### 3.1 Introduction

The methodology illustrates the design adopted to carry out the research, the targeted population, the technique used to collect and analyze data.

### 3.2 Research Design

This gives a generalized plan and arrangement of the study so devised in the mind of the researcher as to secure convincing solution to research questions (Ogula, 2005). A descriptive study involves establishing the rate at which something occurs over a given period of time or the connection involving the variables (Cooper & Schindler, 2008). Descriptive study design intends to gather detailed facts by means of descriptions and is important in establishing variables and logical conclusions.

### 3.3 Target Population

This is **the** total number of items from which an inference is made (Cooper & Schindler, 2006). **The** study **population** was made up of the 64 firms listed at **the NSE as at 31 Decembe**r 2016 thus the study undertook a census approach.

### 3.4 Data Collection

Secondary data was the adopted method. Data on the determinants which include firm size, profitability, leverage and age was collected using a data collection form for a period of five years from 2012 to 2016. Secondary data on the compliance with IFRs was collected using a checklist for a period of five years from 2012 to 2016.

## 3.5 Data Analysis

**Descriptive** design was the preferred method of data analysis and inferential statistic with the help of the SPSS. Descriptive statistical tools entailed the mean, standard deviation and other summary statistics. Inferential statistics entailed correlation and regression analysis, which was employed to determine the relationships.

### 3.5.1 Analytical Model

The regression equation for the study was:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon$$

Where:

Y = Compliance with IFRS, which was measured using the Beest, Braam and Boelus (2009) disclosure index. The index was computed from quality of financial reports, which comprises of relevance, faithful representation, comparability and understandability. The index is determined as follows

$$DI = \frac{\sum_{i=1}^{m} di}{\sum_{i=1}^{n} di}$$

Where, $DI$ = disclosure index, $m$ = number of items actually presented, $n$ = number of total possible items that apply, $di$ = index item i, 1 if the information (item) is supplied (disclosed) and 0 otherwise

$\beta_0$ = Constant

$X_1$= Firm size measure using the natural log of assets

$X_2$ = Profitability measure using the return on assets

$X_3$ = Leverage measure using debt ratio

$X_4$ = Age of the firm measured by the number of years the firm has been in operation

$\beta_1$ - $\beta_4$ = Regression coefficients

$\varepsilon$ = Error Term

## 3.6 Diagnostic Tests

The study undertook the following diagnostic tests

### 3.6.1 Normality

Normality tests are used to determine if a data set is well-modeled by a normal distribution and to compute how likely it is for a random variable underlying the data set to be normally distributed. Non-normally distributed variables can distort relationships and significance tests Normality was tested using skewness and kurtosis where the range of -1 and +1 was considered respectively.

### 3.6.2 Multicollinearity

Multicollinearity is a phenomenon in which one predictor variable in a multiple regression model can be linearly predicted from the others with a substantial degree of accuracy. In this situation, the coefficient estimates of the multiple regression may change erratically in response to small changes in the model or the data. Multicollinearity was determined using the variance inflation factors (VIF) and tolerance levels.

### 3.6.3 Autocorrelation

Autocorrelation, also known as serial correlation, is the correlation of a signal with a delayed copy of itself as a function of delay. Informally, it is the similarity between observations as a function of the time lag between them. In this study, auto correlation was determined using the Durbin Watson test.

### 3.6.4 Homoscedasticity

This is also known as homogeneity of variance. In statistics, the homoscedasticity assumption refers to equal variance of errors across all levels of the independent variables. The homogeneity of variance will be determined through the F statistics and the squared residuals on the independent variables.

## 3.7 Tests of significance

The coefficient of determination ($R_2$) was used to measure the extent to which the variation in efficiency was explained by the variations in its determinants. F-statistic was also computed at 95% confidence level to test whether there was any significant relationship between the independent and dependent variables. The *t-test* was used for testing, the significance of the variables.

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# CHAPTER FOUR: DATA ANALYSIS, RESULTS AND INTERPRETATION

## 4.1 Introduction

This section depicts the results of the research and the discussions of the findings. The chapter illustrates the response rate results, correlation, regression and the interpretation of the findings.

## 4.2 Response Rate

The study population undertook a census of the 64 firms quoted at NSE as at 31 December 2016 and collected secondary data from the firm's financial reports for 5 years 2012-2016. It however managed to obtain data from 60 firms, which had been listed since 2012. The 60 firms led to response rate of 93.75%.

## 4.3 Descriptive Statistics

**Table 4.1 Summary Statistics**

| | **Firm size** | **Profitability** | **Leverage** | **Firm age** | **DI** |
|---|---|---|---|---|---|
| N | 300 | 300 | 300 | 300 | 300 |
| Mean | 16.51107 | .04377 | .12427 | 58.13333 | 2.68723 |
| Std. Deviation | 2.051262 | .106385 | .143090 | 27.468113 | .330299 |
| Skewness | .009 | -1.347 | 1.219 | .366 | -.610 |
| Kurtosis | -.471 | .829 | .707 | -.439 | -.445 |
| Minimum | 12.130 | -.056 | .000 | 8.000 | 1.880 |
| Maximum | 22.090 | .390 | .570 | 114.000 | 3.130 |

**Source: Research findings**

The results of the summary statistics on table 4.1 shows that the average firm size in terms of natural log is 16.51107 and the minimum and maximum value is 12.130 and 22.090 whereas the average profitability of the firms is 0.04377 and minimum and maximum profitability is -0.056 and 0.390 respectively. The findings further indicate that average leverage of the firms is 0.12427 and the minimum and maximum leverage is 0.000 and 0.570 while the average age of the firms is 58.33 with the minimum and maximum ages being 8 and 114 respectively. The results on the disclosure index (DI) indicate that the average disclosure index is 2.687 and the maximum and minimum values being 1.880 and 3.130 respectively. The skewness and kurtosis findings show that all the values lie within negative and positive one hence the data is normally distributed.

## 4.4 Correlation Analysis

**Table 4.2 Correlations**

| | Firm size | Profitability | Leverage | Firm age | DI |
|---|---|---|---|---|---|
| Firm size | 1 | | | | |
| Profitability | -.033 | 1 | | | |
| Leverage | .008 | -.081 | 1 | | |
| Firm age | -.281** | .151** | -.072 | 1 | |
| DI | -.046 | -.074 | .095 | .147* | 1 |

**. Correlation is significant at the 0.01 level (2-tailed).

*. Correlation is significant at the 0.05 level (2-tailed).

**Source: Research findings**

The study results revealed weak and negative association linking correlation between firm size, profitability and the disclosure index (DI). The results also show weak and direct correlation linking leverage, firm age and the disclosure index.

## 4.5 Regression Analysis

### 4.5.1 Model Summary

**Table 4.3 Model Summary**

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate | Durbin-Watson |
|---|---|---|---|---|---|
| 1 | .215[a] | .046 | .033 | .12752 | 1.478 |

a. Predictors: (Constant), Firm age, Leverage, Profitability, Firm size

b. Dependent Variable: DI

**Source: Research findings**

The regression summary results show that the R square statistic value of 0.046 indicates that 4.6% of variations are from the model. The Durbin Watson statistic of 1.478 lies within the recommended range of 1.25 and 2.5 hence an indication there is no autocorrelation.

### 4.5.2 Analysis of Variance

**Table 4.4 ANOVA**

| Model | | Sum of Squares | df | Mean Square | F | Sig. |
|---|---|---|---|---|---|---|
| 1 | Regression | .232 | 4 | .058 | 3.565 | .007[b] |
| | Residual | 4.797 | 295 | .016 | | |
| | Total | 5.029 | 299 | | | |

a. Dependent Variable: DI

b. Predictors: (Constant), Firm age, Leverage, Profitability, Firm size

**Source: Research findings**

The table above reveals regression model significant and fit to explain the relationship between the considered research variables. This is indicted by the P value of 0.007<0.05 and the f value of 3.565 respectively.

### 4.5.3 Regression Coefficients

**Table 4.5 Coefficients**

| Model | | Unstandardized Coefficients | | Standardized Coefficients | t | Sig. | Collinearity Statistics | |
|---|---|---|---|---|---|---|---|---|
| | | B | Std. Error | Beta | | | Tolerance | VIF |
| 1 | (Constant) | .952 | .069 | | 13.791 | .000 | | |
| | Firm size | -.031 | .009 | -.021 | -3.444 | .006 | .921 | 1.086 |
| | Profitability | -.122 | .070 | -.100 | -1.743 | .084 | .972 | 1.029 |
| | Leverage | .070 | .038 | .105 | 1.842 | .068 | .990 | 1.010 |
| | Firm age | .001 | .000 | .170 | 2.828 | .005 | .898 | 1.114 |

a. Dependent Variable: DI

**Source: Research findings**

The coefficient results reveal that correlation linking firm size and the disclosure index of the firms listed at the NSE is negative and significant but the relationship between profitability and the disclosure index of the listed firms in negative and insignificant. The results also show that the relationship between leverage and the disclosure index of the listed firms is positive and insignificant but the relationship between the disclosure index and age of the firm listed at NSE is positive and significant. The results of collinearity statistics depict that there is no multicollinearity since all the tolerance value are more than 0.2 and the variance inflation factors (VIFs) are less than 10.

## 4.6 Interpretation of the Findings

The results reveal strong negative correlation linking firm size and the disclosure index of the firms listed at the NSE. This indicates an existence of strong direct correlation linking the size of the firm and compliance with international financial reporting standards by firms quoted at NSE. They further reveal an insignificant and inverse correlation linking profitability and the disclosure index of the firms listed at the NSE. This indicates absence of strong correlation linking profitability and compliance with IFRS by quoted at the Nairobi securities exchange.

Study results reveal an insignificant and direct correlation linking leverage and the disclosure index of the firms listed at the NSE. This indicates weak relationship linking leverage and compliance with IFRS of firms quoted at NSE. The results show strong and positive correlation linking age of the firm and the disclosure index of the firms listed at the NSE. This reveals an existence of strong correlation linking the age of the firm to its compliance with IFRS by firms listed quoted at NSE.

In similarity to the above findings, Uyar, Kılıç and Gökçen (2016) established, training staff, foreign ownership, and firm size influence IAS/IFRS compliance. Appiah at al. (2016) revealed an existence of direct correlation linking firm’s compliance to firm’s age.

# CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS

## 5.1 Introduction

The section entails the summary of the study, the conclusions and recommendations as well as the study limitations.

## 5.2 Summary

The study aimed at establishing the determinants of IFRS compliance by firms quoted at NSE. The private interest theory, theory of corporate financial management and the agency theory were explored as the key theories for the study. The independent variables of the study comprise of firm size, profitability, leverage and firm age while the dependent variable will be compliance with IFRS. The study population undertook a census of the 64 firms quoted at the Nairobi Securities Exchange as at 31 December 2016 and collected secondary data from the firm's financial reports for 5 years (2012 to 2016). The study however managed to obtain data from 60 firms, which had been listed since 2012. The 60 firms led to response rate of 93.75%.

The results of the summary statistics revealed that the average firm size using natural log was 16.51107 whereas the average profitability of the firms was 0.04377 respectively. The findings further revealed that average leverage of the firms was 0.12427 while the average age of the firms was 58.33 respectively. The results on the disclosure index (DI) established that the average disclosure index was 2.687. The results of correlation analysis established that there was a weak and inverse association linking firm size,

profitability and the disclosure index but a weak and positive correlation between leverage, firm age and the disclosure index.

The regression summary results revealed that 4.6% of the variation were caused by the independent variables and the adopted regression model was significant and a good predictor of correlation linking dependent to independent variable. The coefficient results revealed that correlation linking firm size and the disclosure index of the firms listed at the NSE was negative and significant but the relationship between profitability and the disclosure index of the listed firms was negative and insignificant. The findings also revealed that the relationship between leverage and the disclosure index of the listed firms was positive and insignificant but the relationship between the disclosure index and age of the firm listed at NSE was positive and significant.

## 5.3 Conclusions

The study findings established an existence of strong inverse correlation linking firm size and the disclosure index of the firms quoted at NSE. Thus, the study concludes an existence of strong correlation linking firm size to compliance with IFRS by firms quoted at NSE. The research results found an insignificant and negative relationship between profitability and the disclosure index of the firms listed at the NSE. Thus, coming to conclusion that there is no significant correlation linking profitability to IFRS compliance by firms quoted at NSE.

The research findings also found an insignificant and positive relationship between leverage and the disclosure index of the firms listed at the NSE. Thus, no significant association linking leverage and compliance with IFRS by firms quoted at NSE. The

results of the study found a strong and positive correlation linking age of the firm and the disclosure index of the firms quoted at NSE. Thus, the conclusion of a strong correlation linking the age of the firm and compliance with international financial reporting standards by firms quoted at NSE.

## 5.4 Recommendations

This study concluded that there was a significant correlation linking firm size and compliance with IFRS by firms quoted at NSE. The study thus recommends that the management of small sized firms should also invest resources towards the adoption of IFRS since this will ensure that their financial reports are relevant, faithfully presented, comparable and understandable

The study concluded that there was weak correlation linking profitability and compliance with IFRS by firms quoted at NSE. The study however recommends that the management of listed firms should ensure they comply with international financial reporting standards whether their firms are profitable or not.

The research concluded an existence of weak correlation linking leverage and compliance with IFRS firms quoted at NSE. It therefore recommends the management of should ensure that they adopt and comply with international financial reporting standards whether they finance their firms using leverage or equity.

The results of the study concluded an existence of strong correlation linking age of the firm to compliance with IFRS by firms quoted at NSE. Therefore making recommendation management of young firms should also invest resources towards the

adoption of IFRS since this will ensure that their financial reports are relevant, faithfully presented, comparable and understandable.

## 5.5 Limitations of the Study

The context of this study was firms listed at the NSE since they are required to publish their financial reports and also attached notes on how they arrived at various accounting figures and estimates. The findings therefore are limited to listed firms. The findings also cover the considered study period, which was from 2012 to 2016. Additionally, the study assessed the compliance to all international financial reporting standards and not to a specific component of the IFRS.

## 5.6 Suggestion for Further Research

This study was carried out on firm size, profitability, leverage and firm age as the key determinants of compliance with IFRS by quoted firms. The study however found that the four factors accounted for 4.6% of the compliance to IFRS By listed firms. Thus recommends an additional study, which covers both quantitative factors like corporate governance practices and qualitative factors like the experience of employees, management support among other factors.

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# APPENDICES

## Appendix I: Data Collection Sheet

| Year | 2016 | 2015 | 2014 | 2013 | 2012 |
|---|---|---|---|---|---|
| Total assets | | | | | |
| Net income | | | | | |
| Total debt | | | | | |
| Number of years the firm had been listed | | | | | |

## Appendix II: Quality of Financial Reporting Checklist

**Scores Scale: 1**- Disclosed, **0**- Not disclosed

| **Relevance** | **Score** |
|---|---|
| a. Disclosures forward-looking information in the annual reports | |
| b. Disclosure of information in terms of business opportunities and risks | |
| c. The usage of fair value as measurement basis | |
| d. Provision of feedback information on how various market events and significant transactions affected the company | |
| **Faithful Presentation** | |
| a. Explanations on the assumptions and estimates are clearly made | |
| b. Explanations on the choice of accounting principles are clearly made | |
| c. Positive and negative events have been highlighted in a balanced way when discussing the annual results | |
| d. Disclosure of information on corporate governance issues | |
| **Understandability** | |
| a. The annual report is a well organized | |
| b. The notes to the balance sheet and the income statement are clear | |
| c. Graphs and tables clarify the information presented | |
| d. Use of language and technical jargon is easy to follow in the annual reports | |
| **Comparability** | |
| a. The notes to changes in accounting policies explain the implications of the change | |
| b. The notes to revisions in accounting estimates and judgments explain the implications of the revision | |
| c. The results of current accounting period are compared with results in previous accounting periods | |
| d. Information in the annual report is comparable to information provided by other organizations | |