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## ACCOUNTING, CORPORATE GOVERNANCE & BUSINESS ETHICS | RESEARCH ARTICLE

# IFRS compliance, corporate governance and financial reporting quality of GSE-listed non-financial firms

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**Abstract:** The adoption of International financial reporting standards (IFRS) has been presented in several empirical literature as a factor that could improve the quality of financial reports. However, Ghana has not attained the desired levels of financial reporting quality after the adoption of IFRS. Literature reveals that lack of proper enforcement of these high-quality standards may result in limited compliance and will undermine the effectiveness of these standards in terms of attaining high-quality financial reports. This study therefore argues that the relationship between IFRS compliance and reporting quality revolves around some enforcement mechanisms like corporate governance structures. In view of that, by using random effect estimation technique, this study examined the role of corporate governance in the relationship between IFRS compliance and the reporting quality of firms listed on the Ghana Stock Exchange (GSE). The study found that the right corporate governance mechanisms will enhance the positive effect of IFRS compliance on

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### PUBLIC INTEREST STATEMENT

Most countries have not witnessed the expected improvement in the quality of preparation and presentation of annual reports after the adoption of the IFRS. Thus the empirical evidence on the relationship between IFRS and reporting quality is inconclusive. This is partly due to the fact that IFRS adoption does not equal compliance. Therefore, in this study, we advocate for actual compliance to the IFRS in order to ensure higher levels of reporting quality of firms listed on the Ghana Stock Exchange. In order to ensure IFRS compliance, one of the enforcement mechanisms we advance in this paper is corporate governance.

reporting quality. This study further recommends that to gain an appreciable level of public confidence in the annual reports of firms listed on the GSE, the audit committee's independence and the board's independence should be strengthened to ensure that management does not only adopt IFRS, but that the standards are actually complied with.

**Subjects:** 50.6.1 Economics; 50.6.3 Finance; 50.6.4 Business, Management and Accounting

**Keywords:** IFRS; compliance; reporting quality; corporate governance

## 1. Introduction

Corollary to the 2007 financial crisis, many countries have heightened the importance of ensuring accountability and transparency in financial transactions. Thus many jurisdictions worldwide have emphasised the use of compulsory or voluntary disclosure requirements through several conceptual and legal frameworks. Since business activities of most firms transcend national boundaries, there was the need to adopt a uniform accounting regulations worldwide, to ensure comparability and transparency in accounting transactions. Thus, the International Financial Reporting Standards (IFRS), which was developed by the International Accounting Standards Board (IASB), was intended to be used worldwide to harmonise and guide the preparation and presentation of financial statements in various jurisdictions.

As at 2018, 158 countries worldwide had adopted the IFRS. This therefore, depicts that the stakeholder perspective of corporate governance is gaining more prominence in corporations. The argument of the stakeholder perspective of corporate governance is that management of a firm has the duty to meet the interests of all parties who have a stake in the firm. As a matter of evidence, one of the key interests of most stakeholders of a firm is their need for information. For instance, shareholders need information on the profitability of firms to fulfil their expectations of dividends. The government through the tax authorities need information to know the amount of tax revenue to expect from firms, and suppliers need information to know the credit worthiness of firms. Also, when existing or potential investors are making decisions about buying, selling or holding equity and debt instruments, they will depend on the returns that they expect from the investment in those instruments. These expected returns are estimated using the information disclosed by existing financial statements. Thus, accurate decisions of all these various stakeholders will depend on the level of financial reporting quality.

Entities therefore, have the duty to prepare financial statements for the purpose of providing general information that is useful to various stakeholders in making economic decisions (Baksaas & Stenheim, 2019). According to IASB (2010), the primary objective of financial reporting is to provide high-quality financial reporting information concerning economic entities, primarily financial in nature, useful for economic decision-making. Financial statements also reveal the extent to which management has discharged its duty to use the entity's resources effectively and efficiently. Sloan (2001) posited that financial statements provide first source of information about a firm and that in order for financial statements to meet the diverse needs of users, it is necessary that they must also be of high quality.

In consequence of the potential benefits of high-quality financial reports, strategies aimed at enhancing the quality of financial reports have become imperative to international accounting organisations as well as governments of developing countries (see Elkins & Entwistle, 2018; Hellman et al., 2018; IASB, 2019a; Ofoegbu & Odoemelam, 2018). One of such strategies that have been adopted by several countries worldwide and has dominated accounting literature is IFRS adoption. On the empirical front, studies like Odoemelam et al. (2019), Meeks and Swann (2009), Agyei-Mensah (2013), and Amidu et al. (2016) have argued a positive relationship between IFRS adoption and financial reporting quality. Notwithstanding, studies like Jeanjean and Stolowy (2008), Lin et al. (2012), and A. S. Ahmed et al. (2013) rather find that reporting quality deteriorates

with the adoption of IFRS. Still, another strand of literature finds no significant improvement in reporting quality after the adoption of IFRS (see Christensen et al., 2015; Kao, 2014).

In this study, we advance two main reasons for the inconsistency in empirical literature. First, although literature on reporting quality (for instance, Armstrong et al., 2010; Barth et al., 2008; Kothari, 2000) theoretically links the quality of accounting information to the adoption of accounting standards, the empirical discourse on the relationship between actual compliance to IFRS and reporting quality is limited. The intuition here is that, actual compliance to the IFRS will yield better outcomes than mere adoption. Second, following the argument of Armstrong et al. (2010), lack of proper enforcement mechanisms can lead to variations in the implementation of IFRS, which eventually results in increase in opportunistic managerial discretion, thus undermining the effectiveness of IFRS in producing high-quality information. Therefore, it cannot be assumed that IFRS adoption will necessarily lead to high-quality financial reports in all IFRS jurisdictions, especially ones that are characterised by weak enforcement mechanisms.

In attempt to resolve the debate on the relationship between IFRS and reporting quality, we argue that the relationship between IFRS and reporting quality revolves around some enforcement mechanisms in every IFRS jurisdiction. In view of that, in accounting literature, differences in reporting quality have been attributed to differences in corporate governance. It has been established that several corporate governance structures matter for reporting quality (Abbott et al., 2000; Adams & Ferreira, 2003; K. Ahmed et al., 2006; Campbell & Mínguez-Vera, 2008; Chen, Cheng & Wang, 2014; Cornett et al., 2008; Jimeno & Redondo, 2008; Kukah et al., 2016; Nelson & Devi, 2013; Peasnell et al., 2005; Vafeas, 2000). Following this, we argue that effective corporate governance structures set the centre stage for IFRS to effectively fashion out high level of reporting quality.

Thus this study deviates from existing studies that examine the relationship between IFRS and financial reporting quality, and the relationship between corporate governance and financial reporting quality, to examine the role corporate governance plays in the relationship between IFRS and reporting quality. Even though recent literature has highlighted the importance of strong corporate governance structures due to several corporate scandals, it is yet to be established how corporate governance can influence the relationship between IFRS and financial reporting quality. Therefore, to fill literature gaps and heighten the understanding of the relationship between IFRS and financial reporting quality, there is the need to conduct studies on this issue by examining how actual compliance to IFRS enhances reporting quality, and how corporate governance enhances the relationship between IFRS compliance and financial reporting quality in a developing economy context.

Ghana is of a particular interest to conduct this study due to a number of reasons. First, according to the Report on the Observance of Standards and Codes (ROSC, 2014) by the World Bank, although Ghana has made some progress in the adoption of IFRS, more work needs to be done to improve reporting quality, especially in the area of compliance to the IFRS. Also, literature on IFRS compliance in Ghana so far have focused on the level of compliance and how the level of compliance is associated with company attributes such as size, profitability, leverage, firm age, auditor type, internationality and industry type (see Marfo-Appiah et al., 2016; Yiadom & Atsunyo, 2014), but have ignored how it could spur up the level of financial reporting quality. Finally, the issue of corporate governance has become a topical issue after the collapse of several corporations in Ghana in recent times.

The rest of the paper is organised as follows. The next section presents a review of theoretical and empirical literature on IFRS, corporate governance structures and financial reporting quality. Afterwards, the paper presents the methodology, the empirical analyses, results and discussions. Finally the paper presents a summary, conclusion and implications for policy and practice.

## 2. Literature review and hypothesis development

### 2.1. IFRS and reporting quality

This study emanates from the stakeholder perspective of corporate governance by Donaldson and Preston (1995). This perspective holds that there exists a wide spectrum of stakeholders, and that managers (who are agents) have the duty to satisfy their needs. Indeed one of the needs common to all stakeholders is their information needs. Thus, to avoid adverse selection and its associated moral hazards due to possible information asymmetry between management and other stakeholders (Akerlof, 1978), accounting literature have highlighted the role of accounting standards in reducing information asymmetry through determination of high-quality financial reporting (see Brüggemann et al., 2013; Charitou et al., 2015; Leuz & Wysocki, 2016; Panaretou et al., 2013; Ramalingegowda et al., 2013; Turki et al., 2016).

The relationship between IFRS and reporting quality has attracted a lot of attention in the accounting literature after the IFRS was introduced. Barth et al. (2008) compared the characteristics of accounting information of a large sample of firms from several countries that had adopted IFRS with firms that had not adopted IFRS, and found that reporting quality is better for IFRS-adopted firms than firms that have not adopted the IFRS. Balsari et al. (2010) examined whether the usefulness and quality of financial reporting had increased because of the global move from national accounting standards to IFRS adoption, and found that IFRS has increased both the timeliness and earnings conservatism dimensions of reporting quality. Rad and Embong (2013) found similar evidence, stating that the IFRS has brought about substantial changes in accounting standards, and thus by employing five different indicators for reporting quality, the results revealed that financial information quality has improved after IFRS adoption. Dayanandan et al. (2016) posited that, the quality of financial reporting has improved after the adoption of IFRS in Europe and across the world, and that the adoption of the IFRS has reduced income smoothing and earnings management across several countries thereby enhancing reporting quality.

A firm-level evidence by Neel (2017) suggested that firms that had adopted IFRS enjoyed the economic benefits of reporting quality. Amidu et al. (2016) analysed the implications of IFRS adoption to accounting information quality and found that the adoption of IFRS has brought about an improvement in the quality of financial reporting among financial institutions. In addition, by using pre and post analysis, Agyei-Mensah (2013) investigated the quality of financial reports before and after adopting IFRS in Ghana and found a financial information disclosure mean of 76.80% for pre-adoption period and 87.09% for post-adoption, depicting only an increase in reporting quality after IFRS adoption.

Although literature reviewed so far points to a favourable relevance of IFRS to reporting quality, other strands of literature believe that IFRS adoption impedes reporting quality while some others believe it is irrelevant to reporting quality. By examining the initial effects of mandatory IFRS adoption on reporting quality of 20 countries, A. S. Ahmed et al. (2013) argued that generally the quality of financial reports decreased after the mandatory adoption of the IFRS. Thus, their study raised doubts about inferences that have been made from previous studies that point out a positive link between IFRS adoption and reporting quality, because improvement in reporting quality may be driven by factors other than merely adopting IFRS. Jeanjean and Stolowy (2008) analysed the effects of the mandatory adoption of IFRS standards on earnings quality, and their findings indicated that the extensiveness of earnings management did not decline after the introduction of IFRS. Thus, their study posited that the adoption of standards are not sufficient conditions to reducing the extent of earnings management, hence other factors like compliance could be important in framing financial reporting quality. The findings of Kao (2014) revealed that the adoption of the IFRS does not significantly influence faithful representation, which is a key aspect of financial reporting quality. Amidu et al. (2016) argued that the mixed evidence presented by various empirical literature could be that IFRS in isolation does not enhance reporting quality unless mechanisms are put in place to ensure compliance to these standards. Ahmed et al. (2013) thus contended that the effectiveness of IFRS

adoption in ensuring reporting quality critically depends on the efficacy of enforcement mechanisms to ensure actual compliance to the IFRS. Based on the ongoing discussions, we hypothesise that:

H<sub>1</sub>: *There is a significant positive effect of IFRS adoption on reporting quality but such effect may be weak without IFRS compliance.*

## **2.2. Corporate governance structures and financial reporting quality**

Various studies have highlighted the importance of corporate governance structures in ensuring high level of reporting quality and thus, it is apparent that corporate governance structures such as board size, board independence, audit committee independence and board diversity affect the level of reporting quality of firms (see Abbott, Park & Parker, 2000; K. Ahmed et al., 2006; Adams & Ferreira, 2003; Campbell & Mínguez-Vera, 2008; Chen, Cheng & Wang, 2014; Cornett et al., 2008; Fakhfakh Sakka & Jarboui, 2016; Jimeno & Redondo, 2008; Kukah et al., 2016; Nelson & Devi, 2013; Peasnell et al., 2005; Vafeas, 2000). We therefore discuss the relationship between these corporate governance structures and reporting quality in the subsequent subsections.

### *2.2.1. Board size and reporting quality*

Extant literature has emphasised the importance of board size in ensuring financial reporting quality. Vafeas (2000) found that larger boards are less effective in their monitoring responsibilities, as it will be spread among many directors. One of the reasons argued is that larger boards may find it difficult in reaching decisions when it comes to producing high-quality reports, and also due to the mere size of the board there is less personal responsibility assumed by each director (Vafeas, 2000). Beasley (1996) earlier on contended that increases in board size are likely to result in increases in fraudulent financial statements. Thus K. Ahmed et al. (2006) rather found that smaller boards are more effective in ensuring high level of reporting quality.

### *2.2.2. Board independence and reporting quality*

Board independence has been identified in literature as one of the corporate governance variables that enhances reporting quality. Peasnell et al. (2005) suggested that the effectiveness of monitoring responsibilities of boards depends on the number of independent directors on a board, and advocates for a higher representation of independent directors because they are more independent and effective in their monitoring duties. Moreover, Cornett et al. (2008) found that independent directors bring greater experience to the firm in terms of their monitoring activities. Osma and Noguera (2007) earlier found similar evidence that board members who are independent of management are very instrumental to the governance of a company, predominantly, in relation to fraud and discretionary accounting accruals prevention. Again Klein (2002) found that increases in the number of independent board members represented on a board leads to reduction in the magnitude of earnings management. Xie et al. (2003) suggested that when there are a high number of independent board members, they serve as a sort of check on managers' behaviour. This therefore leaves managers no room to manipulate or manage the earnings to communicate a false state of the companies' financial performance and position, but will rather ensure that reported financial statements represent the true financial state of the firm.

This is particularly essential because Xie et al. (2003) argued that to solve the agency problem in firms, the board of directors should be independent of the firm. Peasnell et al. (2000) also explained that the availability of independent directors is good in constraining the manipulations of discretionary accruals. Also, Chen et al. (2014) posited that higher level of board independence will check the manipulations that occur in financial statements. This is because, relative to the work of dependent board members, the work of executive board members are not faced with familiarity threats and thus, the more independent board members on boards, the lower the propensity of earnings management and the higher the level of reporting quality in the firm.

Based on these discussions, it is apparent that board independence is necessary to enhancing the level of reporting quality.

#### *2.2.3. Audit committee independence and reporting quality*

Audit Committee is one of the important board committees that assist board of directors in their monitoring to ensure transparency and integrity of the financial reporting process (Klein, 2002). According to Section 202 of Sarbanes Oxley, firms are mandated to have an audit committee. Aside the financial expertise of the audit committee members, the independence of members on the committee is necessary for the effectiveness of the committee. Klein (2002) re-emphasised that for an audit committee to be effective in its oversight role, the committee by its make-up, should be independent. This requirement is based on the notion that independent directors are more objective in their analysis of financial statements. Various studies have emphasised the role of the independent audit committee in the discharge of their duties with regards to financial reporting. Abbott, Park and Parker (2000) as well as Klein (2002) found that audit committee independence actually impedes misstatements in financial statements and earnings management. Klein (2002) specifically contended that firms that have more outside directors making up their audit committee had significantly smaller abnormal or discretionary accruals. As such, the more independent members there are on the audit committee, the better it is since it serves as a check on management's opportunistic behaviour. Nelson and Devi (2013) also found similar evidence.

#### *2.2.4. Board gender diversity and reporting quality*

Hillman and Dalziel (2003) argued from the agency theory perspective that female board directors normally incorporate a broad range of ideas, which in turn increases board independence and consequently enhances reporting quality. The inclusion of females in a firm's board of directors incorporates a high sense of responsibility in the decision-making process (Adams & Ferreira, 2003; Campbell & Mínguez-Vera, 2008; Jimeno & Redondo, 2008). Kukah et al. (2016) found a negative relationship between board diversity, gender diversity and earnings management. Gavius et al. (2012) also found evidence of a negative relationship between women on boards and earnings management, which implies a positive relationship between board gender diversity and financial reporting quality.

### **2.3. IFRS reporting quality nexus: the role of corporate governance structures**

Literature on the relationship between IFRS adoption and reporting quality reveals inconclusive results. This means that increases in reporting quality of firms cannot be linked only to the adoption of the IFRS, but also to its compliance and the enforcement mechanisms put in place. The distinction between the adoption of the IFRS and the actual compliance to these standards has become increasingly blatant in the Ghanaian context as financial reports prepared after the adoption of the IFRS are not yielding the expected quality (ROSC, 2014). Hellström (2006) argued that current reporting quality research does not distinguish between the adoption and the implementation of the IFRS. The study further explains that high-quality standards will not be effective in producing high reporting financial statements unless effective control mechanisms are put in place to ensure that these standards are complied.

Several empirical studies have argued that strong corporate mechanisms are required to ensure high reporting quality of firms (see Abbott, Park & Parker, 2000; Adams & Ferreira, 2003; K. Ahmed et al., 2006; Campbell & Mínguez-Vera, 2008; Chen, Cheng & Wang, 2014; Cornett et al., 2008; Jimeno & Redondo, 2008; Kukah et al., 2016; Nelson & Devi, 2013; Peasnell et al., 2005; Vafeas, 2000). Therefore, to enhance the appreciation of the relationship between IFRS and reporting quality, there is worth in conducting studies on this issue by taking into consideration corporate governance structures of firms. In this paper, we employ such an approach to gain insight into the dynamic impact of corporate governance structures on the relationship between IFRS and financial reporting quality of firms listed on the Ghana Stock Exchange, where there have been strenuous efforts to reform and enhance the quality of corporate governance structures. Therefore an important gap that has not been addressed by the extant literature is the role of corporate

governance structures in the relationship between IFRS and reporting quality. This missing link may explain why some jurisdictions have not achieved the full benefits of IFRS.

Thus, our argument is that, the effect of IFRS on reporting quality may depend on absorptive capacities such as the firm's corporate governance structures and as such, IFRS may interact with corporate governance structures to enhance reporting quality. For instance, Krismiaji et al. (2016) found that IFRS adoption in firms with proper board governance increased the value relevance of their financial statements than firms without proper board governance. We therefore take a similar approach to answer some questions on the relationship between IFRS, corporate governance and financial reporting quality. For instance, to what extent will IFRS compliance enhance reporting quality in firms with more independent boards? Further, to what extent will IFRS compliance enhance reporting quality in firms with large or small board size? How would board gender diversity influence the relationship between IFRS compliance and reporting quality? Also, to what extent will IFRS compliance increase reporting quality in the presence of high levels of audit committee independence? In all, although it is evident that the manipulation of corporate governance structures could bring about the needed increase in reporting quality, this argument remains largely unresolved in the extant literature. Consequently, we seek to answer these questions.

### 3. Methodology

Our study examines the relationship between IFRS compliance and financial reporting quality, as well as the moderating role of corporate governance structures in the relationship between IFRS compliance and financial reporting quality of firms listed on the Ghana Stock exchange from the period 2013–2017. The model specification, the data, variable measurement and the estimation procedures are explained in this section.

#### 3.1. Model specification

Model 1 is the baseline model for the relationship between IFRS compliance and financial reporting quality, as well as the relationship between corporate governance structures and financial reporting quality. Following the arguments made by Armstrong et al. (2010) and Kothari (2000), the study expects a positive relationship between IFRS compliance and reporting quality. Also the study expects a significant relationship between corporate governance variables and reporting quality. The first model is specified as follows:

$$\ln RQ_{it} = \alpha_{it} + \beta_1 COMP_{it} + \beta_2 \ln C \cdot GOV_{it} + \sum_{i=3}^n \beta_i Z_{it} + \varepsilon_{it} \quad (1)$$

Where  $\ln RQ_{it}$  represents the natural log of the reporting quality as measured by earnings management of firm  $i$  at time  $t$ ,  $COMP_{it}$  represents the compliance index of firm  $i$  at time  $t$ ,  $\ln C \cdot GOV$  represents the natural log of each of the corporate governance variables of firm  $i$  at time  $t$ ,  $Z$  denotes a vector of the control variables and  $\varepsilon_{it}$  represents the error term.

Model 2 is the baseline model for role of corporate governance structures in the relationship between IFRS adoption and reporting quality. Based on the empirical review, the study expects that the institution of strong corporate governance mechanisms will enhance the effect of IFRS on reporting quality. Thus we make a slight modification to the first model to include interaction terms of each of the corporate governance variables and the IFRS compliance as regressors. The second model is specified as:

$$\ln RQ_{it} = \alpha_{it} + \beta_1 COMP_{it} + \beta_2 (COMP * \ln C \cdot GOV)_{it} + \beta_3 \ln C \cdot GOV_{it} + \sum_{i=4}^n \beta_i Z_{it} + \varepsilon_{it} \quad (2)$$

Where  $\ln RQ_{it}$  represents the natural log of the reporting quality as measured by earnings management of firm  $i$  at time  $t$ ,  $COMP_{it}$  represents the compliance index of firm  $i$  at time  $t$ ,  $\ln C \cdot GOV$  represents the natural log of each of the corporate governance variables,  $COMP * \ln C \cdot GOV$  represents the interaction term of IFRS compliance index and each of the corporate governance variables,  $Z$  denotes a vector of the control variables and  $\varepsilon_{it}$  represents the error term.

### 3.2. Variables and measurement

#### 3.2.1. Dependent variable

In our study, we employed earnings management as an inverse measure of reporting quality. Amidst other measures, this measure is preferred as it responds to the incentives of company information (Burgstahler et al., 2006). Thus we adopted discretionary accrual (DA) as estimated by the Modified Jones Model, and modified by Dechow et al. (1995) as a proxy for earnings management. Also, this measurement was recently employed by Purwanti and Utama (2018).

First of all the value of total accruals is calculated using the formula:

$$TA_{it} = NI_{it} - CFO_{it} \quad (1)$$

Where TA represents total accruals of firm  $i$ , at time  $t$ , NI represents net income of firm  $i$ , at time  $t$ , and CFO represents operating cash flows of firm  $i$ , at time  $t$ .

Next, another regression equation is estimated with the aim of determining the value of the coefficient  $\alpha_1, \alpha_2$  and  $\alpha_3$  using the following equation:

$$TA_{it}/A_{it-1} = \alpha_1(1/A_{it-1}) + \alpha_2[(\Delta REV_{it} - \Delta REC_{it})/A_{it-1}] + \alpha_3(PPE_{it}/A_{it-1}) + \varepsilon_{it}$$

Where  $A_{it-1}$ , denotes lag of total assets of firm  $i$  at time  $t$ ,  $\Delta REV_{it}$  represents change in revenue of firm  $i$  at time  $t$ ,  $\Delta REC_{it}$  change in receivables of firm  $i$  at time  $t$ ,  $PPE_{it}$  represents property, plant and equipment of firm  $i$  at time  $t$ .

Next, the value of non-discretionary accruals (NDA) is obtained by multiplying the coefficient values by certain factors as shown in the formula below:

$$NDA_{it} = \alpha_1(1/A_{it-1}) + \alpha_2[(\Delta REV_{it} - \Delta REC_{it})/A_{it-1}] + \alpha_3(PPE_{it}/A_{it-1})$$

Finally the value of discretionary accruals is calculated using the following formula:

$$DA = TA_{it}/A_{it-1} - NDA_{it}$$

Where NDA represents non-discretionary accruals of firm  $i$  at time  $t$ , and DA represents discretionary accruals.

#### 3.2.2. Independent variables

The level of IFRS compliance was measured as a ratio of what a company presented and disclosed in its annual report, to what it is required to present and disclose for each category of standard, and this is in line with the measurement of Marfo-Yiadom and Atsunyo (2014). That is, the total number of 1 s divided by the total applicable presentation and disclosure requirements. Nonetheless, companies that were not required to disclose certain information in their annual reports were not penalised for not disclosing such information. Further, we adopted the measurement of Gallery et al. (2008) as well as Klein (2002) to measure board independence as the number of non-executive directors divided by the total number of board members. Board size was simply measured by the square of the number of board members in the firm because the relationship between board size and reporting quality is non-linear. We square the board size variable due to its non-linear relationship with reporting quality. The relationship is non-linear because while large board size may be affective in their monitoring duties, escalating board sizes may rather be ineffective in their monitoring duties. Board gender diversity was measured by the number of the women on the board divided by the total number of board members and this is consistent with Kukah et al. (2016). Finally, in line with the measurement of Nelson and Devi (2013) the audit



**Table 1. Variable source and description**

Variable	Measurement	Source
Reporting quality	Total accruals minus non-discretionary accruals	Annual report of listed companies, 2013–2017
IFRS compliance	Total number of disclosed items divided by the total applicable presentation and disclosure requirements	Annual report of listed companies, 2013–2017
Board size	Number of board members squared	Annual report of listed companies, 2013–2017
Board independence	Proportion of non-executive directors out of total board size	Annual report of listed companies, 2013–2017
Audit committee independence	Proportion of outside directors out of the total number of audit committee members	Annual report of listed companies, 2013–2017
Board diversity	Proportion of women directors out of total board size	Annual report of listed companies, 2013–2017
Firm size	Logarithm of total assets	Annual report of listed companies, 2013–2017
Leverage	Long-term debt divided by total assets of firm	Annual report of listed companies, 2013–2017
Big four	Dummy variable, where 0 means that the firm is not audited by any of the Big Four and 1 represents the firm is audited by the big four	Annual report of listed companies, 2013–2017

committee independence was measured by the number of independent non-executive directors on the audit committee divided by the total number of audit committee.

To establish the moderating role of corporate governance structures on the relationship between IFRS compliance and reporting quality, we control for firm specific variables that could possibly have influence on the level of reporting quality in firms. These are firm size, the Big four audit firm, and leverage. These variables were employed in this study because they play an important role in boosting the level of financial reporting quality in firms (see Barton & Simko, 2002; Kukah et al., 2016). Table 1 provides description of the variables and their sources.

### 3.3. Estimation technique

The data was processed by Stata version 13.0 and we employed the random effect estimator based on the results from the Hausman tests. Further, to assess the adequacy of the model, we tested for multicollinearity and joint significance.

## 4. Empirical results and discussions

In this section, we present and discuss the results from the empirical analysis. First, we present the descriptive statistics, which enable us to gain an overview of the data which was used in the empirical analysis. Thereafter, to aid us minimise issues of multicollinearity, we present a correlation matrix. Finally, we present empirical analysis to establish the role corporate governance structures play in the relationship between IFRS compliance and reporting quality.

### 4.1. Descriptive statistics

A descriptive statistics is presented on a sample of 23 non-financial firms listed on the Ghana Stock Exchange out of 41 listed firms. Financial firms were excluded due to their effects on the computation of discretionary accruals. The list of the sample firms listed on the Ghana Stock Exchange included in the study is shown in Appendix A. The descriptive statistics presented in this section is the mean, which is the measure of average, the standard deviation that is the

**Table 2. Descriptive statistics**

Variable	Obs	Mean	Std. Dev.	Min	Max
BIG4	112	.652	.479	0	1
COMP	107	.892	.059	.732	.964
BSS	115	64.609	36.314	9	144
NEDS	90	.711	.243	0	1
WOBS	110	.141	.148	0	.545
IACMS	84	.898	.187	.333	1
TA	107	-3.75e+08	1.96e+09	-1.93e+10	4.54e+07
NDA	67	-1.925	12.967	-106.083	-.007
DA	67	1.985	15.212	-1.157	124.413
Firmsize	104	18.074	3.01	11.429	24.906
LEV	80	.936	4.022	.001	31.212

measure of degree of variability, the minimum and the maximum values for each variable, as well as the number of observations.

BIG4 represents the Big four audit companies, COMP represents compliance index, BSS represents board size squared, NEDS represents board independence, WOBS represents board diversity, IACMS represents audit committee independence, NDA represents non-discretionary accruals, DA represents discretionary accruals, Firmsize represents firm size and Lev represents firm leverage.

From the descriptive statistics in Table 2, the discretionary accrual variable, which is the inverse measure of reporting quality, had an average of 1.985 within the limits of -1.157 and 124.413. This shows that, generally, the sampled listed companies do have a certain level of discretionary accruals. Specifically, some companies have discretionary accrual coefficient as high as 124.13. If the value of DA is not equal to zero, earnings management can occur. If the discretionary accrual value is positive ( $DA > 0$ ), it can be assumed that the company carries out earnings management by increasing its accrual profit reporting. Whereas if it is negative ( $DA < 0$ ), it could signify that the company carries out earnings management by reducing its accrual profit reporting. If the value of  $DA = 0$ , it is assumed that the company does not conduct earnings management. This means that on the average most of the sampled listed firms are carrying out earnings management by increasing their accrual profit reporting. This statistics confirms the report of ROSC (2014), which revealed that although Ghana has made significant progress in reporting quality since the adoption of IFRS, more work needs to be done to improve reporting quality. On the other hand, the sampled listed companies recorded an average compliance of 0.892 within the limits 0.732 and 0.964. This depicts that the sampled listed companies have made significant progress towards compliance to the IFRS in terms of preparation and presentation of financial statements.

As identified by the extant literature, corporate governance could enhance the intensity of how IFRS compliance reduces earnings management and enhances reporting quality. Thus to enable an in-depth understanding of the state of corporate governance indicators in the sampled listed companies, the study also presented the descriptive statistics of each of the four corporate governance structures employed in our study. Board size, board independence, board gender diversity and independent audit committee had averages of 64.069, 0.711, 0.141 and 0.898 respectively. Finally over the period under study, 65.2% of the firm-year observations had their financial statements being audited by one of the big four audit firms while the remaining 34.8% had their financial statements audited by firms other than the big four.

**Table 3. Correlation matrix**

	IDA	COMP	IBSS	INEDS	IWOBS	IACMS	lnLEV	Firm size	BIG4
lnDA	1.0000								
COMP	-0.7688	1.0000							
lnBSS	0.6548	0.4972	1.0000						
lnNEDS	-0.0845	-0.3986	-0.1929	1.0000					
lnWOBS	0.0153	0.4259	-0.1193	-0.2300	1.0000				
lnIACMS	-0.1390	0.2151	0.1924	-0.1137	0.2049	1.0000			
lnLEV	0.672	-0.0651	0.1111	-0.1613	0.2563	0.3250	1.0000		
Firmsize	0.8857	0.4017	0.7514	-0.1012	-0.1811	-0.0654	-0.0107	1.0000	
BIG4	-0.4499	-0.0562	0.4338	-0.3469	-0.1771	-0.3715	-0.0287	0.3604	1.0000

BIG4 represents the Big four audit companies, COMP represents compliance index, lnBSS represents the natural log of board size squared, lnNEDS represents the natural log of board independence, lnWOBS represents the natural log of board diversity, lnIACMS represents the natural log of audit committee independence, lnDA represents discretionary accruals, firmsize represents firm size and lnLev represents the natural log of firm leverage.

#### 4.2. Correlation results

Table 3 presents the pairwise correlation matrix for all the variables employed in our empirical analysis. It could be observed that there could be no multicollinearity problems because the independent variables do not exhibit high correlation of 0.9 as suggested by Kennedy (2003). Rather, it could be observed that most of the independent variables have high pairwise correlation with the dependent variable and this indicates that they have a relationship with the dependent variable. Specifically, discretionary accruals is negatively associated with IFRS compliance, positively associated with board size squared, negatively associated with board independence, positively associated with board gender diversity, negatively associated with audit committee independence, positively associated with leverage, positively associated with firms size and negatively associated with the Big four audit firms.

#### 4.3. Regression results

In this section, we present and discuss our regression results. Table 4 highlights the results of the relationship between IFRS compliance and reporting quality as well as the role of corporate governance structures in the relationship between IFRS compliance and reporting quality. The first regression model in Table 4 reports the results on the relationship between IFRS compliance and financial reporting quality. Subsequently we present the results on the moderating effect of corporate governance structures in the relationship. Model 2 in Table 4 reports the results on the moderating role of corporate governance structures in the relationship between IFRS compliance and reporting quality (see models 2a, 2b, 2 c and 2d). It is worth noting that we employed the natural log of some of the variables in the empirical estimation due to large variations among the data set.

One vital assumption underlying regression models is the assumption of joint significance of the independent variables. Thus, to access whether all the independent variables in models 1–2d of Table 4 were able to jointly predict the dependent variable, a Wald test was performed. The null hypothesis of this test is that the independent variables jointly cannot predict the dependent variable. The *p* values of the Wald test rejected this null hypothesis, which means that all the independent variables in each model jointly explain their dependent variable respectively. This therefore means that all the R-square values in models Table 4 are significant.

4.3.1. *H*<sub>1</sub>: There is a significant positive effect of IFRS adoption on reporting quality but such effect may be weak without IFRS compliance

From the results in model 1, we do find a significant negative ( $\beta = -10.11$ ) relationship between IFRS compliance and the inverse measure of reporting quality. This finding is in line with our first hypothesis

**Table 4. Relationship between IFRS compliance, corporate governance structures, and reporting quality of non-financial firms listed on the GSE**

	Model 1	Model 2a	Model 2b	Model 2c	Model 2d
COMP	-10.11** (3.516)	25.61*** (7.269)	-11.10** (3.528)	-168.6** (58.63)	-101.7** (34.00)
lnBSS	37.24* (18.203)	1548.0** (557.9)	37.29 (22.33)	308.0** (100.9)	258.7** (82.90)
lnNEDS	-33.73* (17.053)	-81.60*** (21.63)	-87.58*** (24.86)	-270.3** (88.20)	-169.8* (76.16)
lnWOBS	29.97* (15.152)	209.8** (67.20)	28.96 (16.06)	5383.0** (1976.1)	356.9** (121.1)
lnIACMS	-114.5* (57.887)	-47.21 (45.94)	-113.4 (61.56)	-406.1*** (114.4)	30,568.1** (11,326.3)
Intbss		-17.08** (6.306)			
Intneds			-0.365 (0.217)		
Intwobs				-54.79** (20.23)	
Intacms					-342.9** (126.6)
lnLEV	9.039* (4.569)	6.608* (2.980)	9.036* (4.571)	6.608* (2.980)	6.608* (2.980)
Firmsize	6.607* (3.340)	34.42** (10.58)	6.588 (4.142)	34.42** (10.58)	34.42** (10.58)
BIG4	-13.87* (7.012)	-176.8* (70.79)	-14.94 (12.74)	-291.7** (113.0)	-308.6** (119.3)
_cons	707.0 (398.6)	-2750.9* (1300.3)	705.7 (398.3)	13,731.1** (4814.2)	7917.5** (2673.2)
N	69	67	66	69	73
R Square	0.8091	0.9707	0.8990	0.8991	0.9712
Wald Chi <sup>2</sup>	35.65	99.48	92.13	99.48	99.48
P>Chi <sup>2</sup>	0.000	0.000	0.001	0.000	0.000

BIG4 represents the Big four audit companies, COMP represents compliance index, lnBSS represents the natural log of board size squared, lnNEDS represents the natural log of board independence, lnWOBS represents the natural log of board diversity, lnIACMS represents the natural log of audit committee independence, lnDA represents discretionary accruals, firmsize represents firm size, lnLev represents the natural log of firm leverage, Intbss represents the interaction term between compliance index and board size, Intneds represents the interaction term between compliance index and board independence, Intwobs represents the interaction term between compliance index and board diversity, and Intacms represents the interaction term between compliance index and audit committee independence.

that IFRS compliance is more effective in ensuring high level of reporting quality than just adoption. The results also support the stakeholder perspective of corporate governance by Donaldson and Preston (1995). Further, this finding is consistent with the arguments of Jeanjean and Stolowy (2008), A. S. Ahmed et al. (2013), and Amidu et al. (2016). This result indicates that actual compliance to IFRS plays a significant role in enhancing the level of financial reporting quality in our sampled listed firms. The practical implication of our findings is that, if managers of our sampled listed firms aim at enhancing the level of financial reporting quality in their firms, they need to ensure high level of compliance to the IFRS.

Following from this finding, we set out to assess whether the presence of corporate governance structures enhances the relationship between IFRS compliance and financial reporting quality in our sampled listed firms. Therefore, we proceeded to interact the corporate governance structures with IFRS compliance to test our argument that corporate governance structures play a key role in the relationship between IFRS compliance and reporting quality. In model 2a, we do find a significant negative ( $\beta = -17.08$ ) effect of the interacting term between IFRS compliance and board size on the level of financial reporting quality. However, by introducing this interaction term, the IFRS compliance variable rather attained a significant positive coefficient of 25.65 as compared to a coefficient of  $-10.11$  in Model 1. This implies that a larger board size has the potential to make IFRS compliance better ensure higher reporting quality but escalating levels of board size could erode such benefits. This result is in line with the argument of Vafeas (2000).

In model 2b, we do find no significant effect of the interacting term between IFRS compliance and board independence on the level of financial reporting quality. However, introducing this interaction term causes the IFRS compliance variable to rather attain a significant coefficient of  $-11.10$  as compared to a coefficient of  $-10.11$  in Model 1. This result provides some evidence that the presence of independent board members will ensure that IFRS compliance translate into the required levels of reporting quality. This result is in line with Peasnell et al. (2005). In Model 2c, we do find a significant negative ( $\beta = -54.79$ ) effect of the interacting term between IFRS compliance and board diversity on the level of financial reporting quality. In addition, the IFRS compliance variable now shows a higher negative coefficient ( $\beta = -168.66$ ) as compared to that of Model 1 ( $\beta = -10.11$ ) in Model 1. This therefore shows that IFRS compliance will better enhance reporting quality in the presence of a higher gender diversified board. This is in line with the argument of Campbell and Mínguez-Vera (2008) and Kukah et al. (2016).

Finally, we find a negative significant ( $\beta = -342.9$ ) effect of the interacting term between IFRS compliance and audit committee independence on the level of financial reporting quality. Further, the interaction term causes the IFRS compliance variable to have higher negative coefficient ( $\beta = -101.7$ ) as compared to its coefficient in Model 1 ( $\beta = -10.11$ ). This means that IFRS compliance will better enhance reporting quality in when a more independent audit committee is put in place. This is primarily because the basic intent of the establishment of an audit committee is to enhance the quality of financial reports. This results is in tandem with that of Nelson and Devi (2013) as well as Klein (2002). In sum, amidst all the interaction terms presented in Models 2a–2d, the interacting term between IFRS compliance and audit committee independence is the highest predictor of reporting quality. This provides some evidence that audit committee independence is the corporate governance mechanism that is directly related to ensuring high level of reporting quality.

In all the models presented in Table 4, firm size had a significant positive effect on the inverse measure of reporting quality. This result corroborates that of Barton and Simko (2002) who found that managers of large-sized firms face more pressures to meet the expectation of stakeholders so they are likely to manage earnings. In all the models in Table 4, firm leverage had a significant positive effect on the inverse measure of reporting quality which indicates that reporting quality decreases with high levels of firm leverage. This findings in line with that of Januarsi et al. (2014) who found that managers of highly leveraged firms can artificially increase reported earnings to improve firm's bargaining power during debt negotiation in order to obtain funds at favourable conditions. Finally, in all the models, we do find a negative effect of the big four on the inverse measure of reporting quality. This means when a firm is being audited by either the big four audit firms (i.e. KPMG, PWC, Ernst and Young or Deloitte); there is low likelihood that the firms will be able to manipulate earnings, and this is in sync with the results of Bédard et al. (2004).

## 5. Summary and conclusions

### 5.1. Summary

Our study sought to examine the role of corporate governance in the relationship between IFRS compliance and the level of financial reporting quality of firms listed on the Ghana stock exchange. Based on the results from the random effect estimations, we do find a strong, significant, positive effect of IFRS compliance on the level of financial reporting quality. Further, our results exhibit a significant moderating effect of corporate governance structures on the relationship between IFRS compliance and the level of reporting quality. These findings give support to our argument that although the level of reporting quality could be enhanced through compliance to IFRS; higher levels of financial reporting quality could be effectively fashioned out as a result of the presence of good corporate governance structures also.

### 5.2. Contributions

Although literature on reporting quality theoretically links the quality of accounting information to the adoption of accounting standards, the empirical discourse on the relationship between actual compliance to IFRS and reporting quality is limited. First, we contribute to extant literature by examining how actual compliance to the IFRS influences reporting quality. Second, following the argument of Armstrong et al. (2010), we examined how proper enforcement mechanisms like corporate governance structures could ensure effective compliance of IFRS so that the expected levels of reporting quality could be achieved. Thus another major contribution of our paper is that it examines how corporate governance structures acts as absorptive capacities in the relationship between IFRS compliance and financial reporting quality.

### 5.3. Implications

Based on the findings, it is recommended that listed firms should ensure strict compliance to IFRS than just mere adoption. However, such efforts could be much more visible if there is an improvement in the strength of the corporate governance structures also. This could be made possible if the Security and Exchanges Commission institute policies aimed at legalising strict adherence to proper corporate governance structures. This will ensure that there is high level of board independence and most prominently audit committee independence. Also, the practice of having more women on corporate boards should be encouraged but with caution such that the conservative nature of women will be channelled into ensuring high levels of reporting quality. Finally, the practice of having more large boards should be encouraged but with caution so that the large board size will rather ensure that IFRS compliance leads to the desired levels of reporting quality.

### 5.4. Limitations

Our study is associated with some limitations. We employed data from 23 non-financial firms listed on the Ghana Stock Exchange out of 41 listed firms and thus, generalising the results to all firms listed on the Ghana stock exchange is quite puzzling. However, this was due to the highly subjective effect that financial firms have on the computation of discretionary accruals. Similar studies could therefore be conducted for financial firms listed on the Ghana stock exchange.

### 5.5. Avenue for future research

First of all, other studies can extend this current study by examining the moderating role played by corporate governance structures in the relationship between IFRS compliance and reporting quality of other firms which are not listed on the GSE. An extension of this study can be conducted for financial institutions listed on the GSE. Other sources and dimensions of corporate governance could also be employed. For instance, further studies can examine the role played by country level corporate governance in the relation between IFRS compliance and reporting quality of firms. Also, the study focused on IAS 1 for the construction index, other studies could look at other standards for compliance measure. Finally, further studies could employ other estimation techniques than those employed in this study.

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## Appendix A.

### List of 23 non-financial firms listed on the Ghana Stock Exchange

1	African Champions Industries Ltd
2	Aluworks Ltd
3	AngloGold Ashanti Limited
4	Aryton Drugs Manufacturing
5	Benso Oil Palm Plantation Ltd
6	Camelot Ghana Ltd
7	ClydeStone Ghana Ltd
8	Cocoa Processing Company
9	Fan Milk Limited
10	Ghana Oil Company Limited
11	Golden Star Resources Ltd
12	Golden WEB
13	Guinness Ghana Breweries Ltd
14	Mechanical Lloyd Company
15	Produce Buying Company Ltd
16	Pioneer Kitchenware Ltd
17	PZ Cussons Ghana Ltd
18	Sam Wood Ltd
19	Starwin Products Ltd
20	Total Petroleum Ghana Ltd
21	Transol Solutions Ghana Ltd
22	Tullow Oil Ghana
23	Unilever Ghana Limited



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