

Antecedents of IFRS Compliance: The Moderating Effect of Audit Quality

Martin Kabwe¹, Erastus Mwanaumo², Henry Chalu³

¹Graduate School of Business, University of Zambia, Great East Road Campus, Lusaka, Zambia

²Graduate School of Business, School of Engineering, University of Zambia, Great East Road Campus, Lusaka, Zambia

³School of Business, University of Dar-es-salaam, Dar-es-salaam, Tanzania

Email address:

Kabweha@yahoo.com (M. Kabwe), Erastus.m.mwanaumo@gmail.com (E. Mwanaumo), hchalu@gmail.com (H. Chalu)

To cite this article:

Martin Kabwe, Erastus Mwanaumo, Henry Chalu. Antecedents of IFRS Compliance: The Moderating Effect of Audit Quality. *Journal of Finance and Accounting*. Vol. 9, No. 6, 2021, pp. 216-229. doi: 10.11648/j.jfa.20210906.12

Received: October 8, 2021; **Accepted:** November 4, 2021; **Published:** November 10, 2021

Abstract: Despite the significant non-compliance with IFRS, most audit reports provide unqualified opinion which brings into question the audit quality in enforcing IFRS compliance. Therefore, the purpose of the study was to examine the antecedents of compliance with IFRS by focusing on the moderating effect of audit quality on the association of firm characteristics and IFRS compliance. The collection of data was done through quantitative content analysis of annual reports of 20 Zambian listed companies and Zambia Institute of chartered Accountants covering the years 2012 to 2018. Being a longitudinal study requiring panel data analysis, a Hausman test was done to choose the model to employ. The Hausman test showed that the random effect model was suitable. Results indicate that audit quality moderates the association of firm characteristics and IFRS compliance. Also, there was a positive association between firm size and compliance with IFRS. There was a negative association between firm profitability and compliance with IFRS. However, there was a statistically insignificant positive association between foreign investors, institutional investors, audit quality and IFRS compliance. The study suggests that large companies are expected to comply more with IFRSs and profitable firms withhold financial information. Audit quality was not impaired probably due to the size of the audit firms and international affiliation. Meanwhile, the influence of institutional investors and foreign investors on IFRS compliance was insignificant probably because both institutional and foreign investors in Zambian listed companies are transient investors without significant incentives to demand financial disclosures and they may have other means to access financial information. The financial reporting regulators should focus on enhancing audit quality for listed companies in Zambia and even in other African countries. Future research can focus on the relevance of IFRS disclosures to the domestic investors in Africa considering the cultural differences both at firm and national-level.

Keywords: Audit Quality, IFRS Compliance, Firm Characteristics, Zambian Listed Companies

1. Introduction

The financial statements that are prepared in compliance with International Financial Reporting Standards (IFRSs) are considered to provide transparent and credible financial information [1]. According to IASB [2], a firm is deemed IFRS compliant when it adheres to all the applicable IFRSs. External auditors provide assurance with regards to the credibility of financial information contained in the company financial reports through independent quality audits, which improves resource allocation and contracting efficiency [3-5].

Therefore, financial statements which has been audited are considered to contain more reliable financial information than those that are unaudited [6].

Audit quality play a vital part in the enforcement of compliance and implementation of IFRS standards [7-9]. Despite the perceived provision of quality audit of financial statements by external auditors, there is still a non-compliance problem with IFRSs as evidenced from research [10-14]. However, despite the significant non-compliance with IFRSs most auditors produce unqualified reports [15-17]. This brings into question the audit quality in enforcing compliance with IFRSs.

The problem of non-compliance is worse for Africa because African countries are plagued with low compliance with global standards such as IFRSs due to the weakness in the institutional and enforcement mechanism [18-20]. In most countries, the financial reporting regulators rely mostly on auditors to enforce compliance with accounting standards such as IFRSs. It can be argued that since the enforcement is weak in developing countries due to weak institutional regulatory setting, audit quality would be the most effective external enforcement mechanism. Ewert and Wagenhofer [21] argue that although enforcement and auditing can be alternatives in a strong enforcement regime, they are complements in a weak regime. Choi and Wong [22] noted that auditors have a relatively more cardinal role to play in the corporate governance system where the legal institutions are weak. However, Stokes and Webster [8] argue that an auditor is more likely to effectively enforce compliance with IFRS standards in a stronger legal institution with investor protection in order to avoid being punished if the misreporting by the client is detected. Therefore, the propensity to enhance the quality of an audit depends on the sanctions auditors are exposed to for misreporting. Nevertheless, the powers to discipline erring firms or auditors by the financial reporting regulators are mild in most countries and auditors just issue generic audit reports which do not achieve the perceived value of the assurance function [23, 24]. Therefore, it is inevitable to conduct empirical studies to determine the association of audit quality and compliance with IFRS.

In Africa, most countries tend to combine professional accounting body and standards enforcement body in one organization. For instance, in Zambia, despite the presence of professional body which is member based and standard body which has got stakeholders' perspective, the standard body is under the professional body. This implies that the Zambia Instituted of Chartered Accountants (ZICA) and the Standards and Regulatory Board (SRB) which was established in 2009 are effective one organization. World Bank [25] pointed out that the SRB is not independent as it reports to the members whom it regulates. Hence, it is not surprising that there is still non-adherence to IFRSs and listed companies receive unqualified audit reports in Zambia [17].

The regulating of corporate financial reporting in Zambia has the features of a thin political market. According to Ramanna [26] the thin political market has two basic features, the first being concentrated commercial interest (special-interest group) with profoundly relevant expertise on the issue at hand. Secondly, the public interest (general interest) is diffuse as the specific issue has a small individual impact on each member of the public and it is not salient in the public's mind. ZICA council runs the affairs of the institutes on behalf of its members. The council comprise of about 60% auditors who are a special interest group with relevant expertise. In addition, the Zambian public has no significant interest in IFRSs compliance by companies. In the thin political market, the special-interest group is informed and unopposed that can capture the political process and opportunistically twist accounting rules. Worse still, the some

audit partners of firms auditing listed companies sit on ZICA council which presents potential conflict of interest and can compromise the audit quality. Therefore, given this context, the study attempted to establish whether audit quality play a part in the enforcement of compliance with IFRS in Zambia.

Furthermore, this situation indicate that concentrating only on external enforcement may not be an appropriate approach because of limited settings of ZICA and SRB. As such this study also considers that looking for other explanatory variables may be crucial. These explanatory variables may include those based on firm characteristics as identified by several studies [27-34, 19]. According to Golan *et al.*, [35] firm characteristics are the firm's resources and objectives which influence the performance of organizations. However, various studies have conceptualized firm characteristics differently which depends on the measures used to describe it [36]. Most of the prior studies on determinants of IFRS compliance have conceptualized firm size, firm profitability, leverage ratio, liquidity, auditor size, internationality and ownership dispersion as firm characteristics influencing the level of IFRS compliance [37]. This study employed audit quality, foreign investors, institutional shareholding, firm size and firm profitability as firm characteristics.

However, studies on the association between firm characteristics and IFRS compliance have produced conflicting results [27, 29, 31, 34, 13, 59]. Notwithstanding the conflicting empirical results, there is also insufficient research on the relationship between a firm characteristics and IFRS compliance focused on developing countries [37, 38]. In Zambia, except for the study by Kabwe *et al.*, [39] which focused on the effect of corporate governance attributes on IFRS compliance, there is hardly any research on the factors influencing compliance with IFRS and the World Bank [25] called for empirical studies on compliance with IFRS in Zambia. Therefore, the purpose of the present study is to examine the antecedents causing IFRS compliance by also focusing on audit quality as a moderating variable in Zambia.

The subsequent parts of the study are as follows: Section two covers the theoretical literature review while section three covers the empirical literature review. Section four provide the hypotheses development. Section five cover the research methods. Section six and seven presents the results and discussion of the research findings respectively. Lastly, section eight conclude the study.

2. Theoretical Literature Review

Studies on antecedents of IFRS compliance focusing on developing countries largely employed agency theory and other capital market theories [37]. However, companies can be coerced to use IFRS and thus, compliance depends on management who act based on the interests of the company stakeholders especially in Africa [40]. Moreover, African countries have inefficient capital markets to echo external reporting and corporate financial reporting may only be of interest to certain stakeholders due to power, legitimacy or urgency and therefore, stakeholder salience theory is

appropriate [40]. On the other hand, different theories can be complemented to produce a range of insights or explanations [41]. Taking a plural rather than a parochial approach to theoretical framings is important [42]. Therefore, the present study combines agency theory, stakeholder salience theory, and positive accounting theory to comprehensively determine factors influencing IFRS compliance in Zambia.

2.1. Stakeholder Salience Theory

The power, legitimacy and urgency that a stakeholder has determine the managers' decisions on the salience stakeholders [43]. Therefore, influencing IFRS compliance is determined by the managers' perception of a stakeholder's power, legitimacy and urgency. Hence, the interaction among these attributes (power, legitimacy and urgency) leads to different stakeholders' categories such as dormant, discretionary, demanding, dominant, dangerous, dependent and definitive [43]. However, some categories of stakeholders may not have interest in IFRS compliance by the companies [40]. Thus, the present study adopts the three categories (discretionary, dominant and definitive) influencing managers in complying with IFRS as identified by [40]:

2.1.1. Definitive Stakeholders

Definitive stakeholders are already members of a firm's dominant coalition with who have power and legitimacy [43]. Therefore, if a definitive stakeholder's demand is urgent such as compliance with IFRS, managers respond to such demands immediately. External auditors have the power and legitimacy to demand for compliance with IFRSs and their claim is urgent. The Company Act 2017 in Zambia requires financial statements of listed companies to be audited before being presented to the shareholders. This implies that auditing is a legal requirement for listed companies in Zambia.

However, some audit partners for firms auditing listed companies sit on ZICA council which may present conflict of interest and compromise the audit quality as evidence by issuance of unqualified audit reports despite substantial non-adherence with IFRSs [17]. Audit quality influence significantly the compliance with IFRSs [7]. Moreover, financial reporting regulatory bodies indirectly enforce IFRS compliance through supervision of audit assurance providers [44]. The quality review of audit assurance providers conducted by financial reporting regulatory bodies would enhance the quality of the audit reports. Realization of the benefits of IFRS adoption depends on the enforcement and implementation of IFRS by higher audit quality and thus, audit quality matters in the enforcement of compliance and implementation of IFRS standards [8].

2.1.2. Dominant and Discretionary Stakeholders

According to stakeholder salience theory dominant stakeholders possess power and legitimacy. Their influence in the firm is guaranteed because of power with legitimacy which they may choose to act on their claims or not. However, management is concerned about their expectations (for instance compliance with IFRSs) because of their power

and legitimacy [43].

Privatization attracted foreign direct investment more especially in developing countries and foreign investors form part of the institutional investors [45]. The role of foreign investors as institutional investors can be explained by two perspectives of the stakeholder salience theory, dominant and discretionary. According to the dominant view, foreign investors may have both power and legitimacy if their shareholding is significant and they may choose to act on their claims (e.g. demand compliance with IFRSs). Bova and Pereira [19] opine that foreign investors compared to domestic investors demand more adherence to globally accepted set of standards to mitigate information asymmetries. Therefore, foreign investors monitor management effectively and demand more compliance with disclosure standards such as IFRSs [46]. However, since foreign investors in Africa have access to internal information through holding key positions, they have less interest in adherence to the laws or IFRSs [40].

On the other hand, according to the discretionary view, foreign investors have legitimacy without power to influence IFRS compliance or urgency to make demands if their shareholding is insignificant or widely dispersed. This is because minority interests have legitimacy to demand compliance with IFRSs, but fail short of power and urgency to compile management for such a demand [40].

Pension funds, insurance companies and other financial institutions form part of institutional shareholders and normally hold a significant equity stake. These institutional investors play a vital role in the financial market such that their investment decisions can affect movement in share prices and management disclosure policies [47]. The significant equity stake in a firm by institutional investors makes them dominant stakeholders as they have legitimacy and power of which they may then opt to act on their demands (IFRS compliance) or not. [40] Postulate that shareholders with significant equity stake possess power and legitimacy, and can have the urgency to demand compliance with IFRS. However, compliance with disclosures may be of little interest to dominant shareholder [48]. As a result, Glaum *et al.*, [13] posits that an inverted U-shaped relationship may exist between ownership concentration and disclosure quality and hence compliance with disclosure requirements [49]. However, according to stakeholder salience theory, management is expectant of dominant stakeholders' claims such compliance with IFRSs and will address them [43].

Despite the expectation that institutional shareholders influence IFRS compliance, Eng and Mak [50] posit that institutional shareholding does not positively influence IFRS compliance. Conversely, some studies indicated a positive relationship between institutional ownership and the level of disclosures [51, 52].

2.2. Positive Accounting Theory

The bonus plan hypothesis, the debt covenant hypothesis and the political cost hypothesis are the three hypotheses

under Positive Accounting Theory (PAT). According to political cost theory, companies disclose information voluntarily to reduce political costs because regulatory authorities make decisions based on the disclosed information [53]. The political cost theory conjecture that large firms compared to small firms opt for accounting methods that defer current earnings to the future periods. Higher reported earnings can put the company (especially large firms) in the political limelight and can lead to new taxes or regulations. Besides, certain industries are highly regulated by the government due to their nature.

To avoid or reduce high political costs and visibility, companies may use financial information or accounting changes through improved IFRS compliance which act in a way to limit manager's accounting choice [54]. Companies in countries where there is a lot of government meddling are mostly reluctantly display huge profits to avoid regulations and therefore expedite bad news recognition [55, 56].

Some empirical studies have shown a positive association between IFRS compliance and firm size [57-59, 12, 11, 29]. Meanwhile, Karim and Ahmed [60] revealed a negative association between IFRS compliance and firm size. Similarly, [61, 16] indicate no relationship between IFRS compliance and company size.

In Zambia, mining companies form part of large firms and contribute significantly (account for about 70% of exports) to the economy [62]. There is demand from stakeholders that large companies from extractive industries and others to improve on accountability and transparency through disclosure of information in Zambia [63]. Therefore, large firms in Zambia are likely to adhere to IFRS disclosures to avoid political costs and because of lower information processing cost compared to small firms.

2.3. Agency Theory

Agency theory assumes that ownership and control of an entity are separate which creates an agency relationship between the shareholders and management [64]. Managers are agents of the shareholders charged with the responsibility of running the companies on behalf of the shareholders. Conflict of interest between managers and shareholders can arise and to remedy this, the principal incur agency costs such as monitoring and bonding [65, 64, 72]. The preparation of financial statements reduce the agency problem through disclosure of detailed financial information (comply with IFRS disclosures) which form part of monitoring costs [64]. Therefore, managers of profitable companies are expected to provide more financial disclosures to signal their excellent stewardship, increase investors' confidence and justify compensation [66, 67].

However, the studies show that the association between IFRS compliance and profitability is varied. Some extant empirical evidence show a negative association between IFRS compliance and profitability [12, 58, 59]. Meanwhile, other studies show a positive relationship between IFRS compliance and profitability [68, 11, 34].

3. Empirical Literature Review

3.1. Audit Quality

Prior studies mainly employed audit type (big or small) and international affiliation of audit firm as proxy for audit quality. The empirical evidence show that audit type or audit firm with international affiliation positively influence compliance with IFRSs. For instance, Ballas *et al.*, [28] in Greece found that there is a positive relationship between having international big auditing firm and IFRS compliance. Ebrahim [69] in Egypt examined compliance and enforcement of IFRSs as well as the effect of independent audit quality on IFRS compliance. The results showed evidence that IFRS compliance was significantly associated with internationally affiliated audit firm. Samaha and Stapleton [58] in Egypt also found that being audited by an international audit firm was a critical cause for compliance with accounting standards.

In Bahrain Alrawahi and Sarea [70] sampled 36 listed firms and found that only audit type have a significant positive relationship with IFRS compliance. In Ghana Appiah *et al.*, [32] sampled 31 listed firms and found a positive significant association between the level of IFRS compliance and auditor type. In Poland Bialek-Jaworska and Matusiewicz [71] sampled 36 listed firms and found that auditor type has a positive statistically significant relationship with IFRS disclosure. In Australia Bepari *et al.*, [34] indicated that audit type (quality) is a major factor influencing IFRS compliance. In Turkey Misirlioğlu *et al.*, [10] found that the type of auditor influence positively the accounting standards disclosures.

In Jordan Al-Akra *et al.*, [68] sampled 80 non-financial listed companies and found that auditor size exert a positive effect on compliance with IFRS. In Kuwait, [11] used a sample of 121 companies and found that auditor type is significantly associated with IFRS compliance. Karim and Ahmed [60] in Bangladesh used a sample of 188 companies and the study revealed that the degree of compliance is strongly associated with the size of auditors. In China Chen and Rezaee [73] found that the quality of audit that mediates the association between internal corporate governance and IFRS convergence.

Although the preceding review show a positive influence of audit type on IFRS compliance, Fekete *et al.*, [57] in Hungarian found no significant association between audit type and the level of compliance with IFRS.

3.2. Foreign Investors

Prior research on the association between foreign investors and IFRS compliance indicates conflicting evidence. For instance, Pownall and Wieczynska [29] found that firms with foreign operations and more analyst following were more likely to comply with IFRSs in Europe. In Turkey studies found that foreign ownership is one of the significant determinants of IFRS compliance [31, 10]. In Brazil, Sônia and Baptista [74] revealed that firms with more foreign board members have a higher compliance with IFRS3 disclosures. Abdullah *et al.*, [75] revealed that foreign investors have positive impact on market value. However, Almaqtari *et al.*, [76] found a statistically

significant negative influence of foreign investors on the level of IFRS compliance in the Kingdom of Saudi Arabia and Oman but a positive significant influence on IFRS compliance in the case of the United Arab Emirates.

In Africa, Bova and Pereira [19] in Kenya found that foreign investors was associated positively with IFRS compliance, and the greater the foreign ownership the greater IFRS compliance. Also, Ebrahim and Fattah [77] in Egypt found evidence that having foreign board members on the board improves IFRS compliance.

3.3. Institutional Shareholding

Institutional shareholders form part of the ownership structure. However, the results on the association between institutional ownership and IFRS compliance is also conflicting. The reason for the differences in the results regarding the impact of ownership structure on IFRS compliance across countries could be influenced by the differences in the legal origins [13]. For instance, Ballas *et al.*, [28] found that closely-held firms show a higher IFRS compliance. Meanwhile, Rahman and Hamdan [78] in Malaysia found that there is no significant association between outside blockholders' ownership and the level of IFRS compliance. Al-Sartawi *et al.*, [79] in Bahrain found that there is a negative association between ownership of top stockholders, and compliance with IAS 1 disclosures. In Jordan [68] found that ownership diffusion is negatively associated with IFRS compliance. Bialek-Jaworska and Matusiewicz [71] found that shareholder diffusion does not have any statistical relationship with IFRS disclosures. In the Gulf Co-operation Council member states Al-Shammari *et al.*, [12] found that there was no significant connection between ownership diffusion and IFRS compliance. Also, Juhmani [80] in Bahrain found that there was no association between blockholder ownership, managerial ownership, and government ownership with IFRS compliance.

The impact of ownership structure on the level of IFRS compliance has also revealed conflicting results in Africa. For instance, Sellami and Fendri [81] found a significant negative association between concentrated ownership and the level of compliance with related party transactions (IAS 24) disclosures and the more concentrated the less compliant. However, Agyei-Mensah [82] in Ghana also investigated the compliance with IAS 24 and found that the level of compliance with related party transactions (IAS 24) disclosures was influenced by ownership concentration. Samaha and Stapleton [58] in Egypt found that ownership concentration was also associated with the level of IFRS compliance. Also Ebrahim and Fattah [77] in Egypt found evidence that institutional ownership improves compliance with IFRS disclosure requirements.

3.4. Firm Size

The empirical evidence of firm size as a determinant of IFRS compliance is inconsistent. For instance, Pownall and Wieczynska [29] found that larger firms in Europe were likely to comply with IFRSs. In Austria Bepari *et al.*, [34] found that there was a relationship between firm size and

IFRS compliance. In Poland Bialek-Jaworska and Matusiewicz [71] found that firm size has a positive association with IFRS compliance. Contrary, Ballas *et al.*, [28] in Greece found that firm size does not influence IFRSs disclosure compliance. Almaqtari *et al.*, [76] found that firm size was associated negatively with IFRS compliance in the Kingdom of Saudi Arabia and a positive significant effect at the level of IFRS compliance in Oman, but there was an insignificant effect in the case of the United Arab Emirates. In Europe, Glaum *et al.*, [13] did not find a significant association between firm size and IFRS compliance.

The empirical evidence from the developing countries on the relationship between firm size and the level of IFRS compliance is also conflicting. For instance, Al-Shammari *et al.*, [12] sampled 137 listed firms in the Gulf Co-operation Council member states and the study showed that firm size had a significant positive effect on IFRS compliance. In Malaysia Abdul-Rahman *et al.*, [27] sampled 105 manufacturing companies and found that only firm size had a positive significant association with IFRS compliance. However, [60] in Bangladesh found a negative significant association between firm size and the level of compliance with IFRS disclosures. In Indonesia Ernawati and Aryani [83] found an insignificant association between firm size and compliance with related party transactions (IAS 1).

Empirical evidence from African countries related to the association of firm size and IFRS compliance is not different from other developing countries across the globe i.e. results are inconclusive. For instance, Samaha and Stapleton [58] in Egypt found that firm size is associated with accounting standards disclosures. In Ghana Appiah *et al.*, [32] sampled 31 listed and found a positive significant association between firm size and IFRS compliance. In Malawi Taurigana and Chithambo [33] found there was a positive association between firm size and IFRS compliance. However, Tsegba *et al.*, [30] in Nigeria found that there is no significant association between firm size and the level of IFRS compliance.

3.5. Firm Profitability

The prior studies show that the association between firm profitability and IFRS compliance is also conflicting. In Austria Bepari *et al.*, [34] found that firm profitability had a positive significant relationship with the level of compliance with IFRS disclosures. Meanwhile, Bialek-Jaworska and Matusiewicz [71] in Poland found a negative statistically significant relationship between profitability and IFRS compliance disclosures. Also, Ballas *et al.*, [28] in Greece found that firms' profitability does not influence IFRSs disclosure compliance.

The prior study results on the impact of firm profitability on IFRS compliance from developing countries are also mixed. Alrawahi and Sarea [70] in Bahrain found that profitability had a positive and significant association with compliance with IFRS disclosure requirements. Al-Mutawaa and Hewaidy [11] used a sample of 121 companies and found that profitability was significantly associated with IFRS compliance. Al-Akra *et al.*, [68] in Jordan found that profitability exerts a significant

positive effect on IFRS compliance. Meanwhile, Abdul-Rahman *et al.*, [27] in Malaysia, found a negative significant association between profitability and the level of compliance with IFRS disclosures. Uyar *et al.*, [31] in Turkey found no significant relationship between profitability and the level of IFRS compliance.

The association between firm profitability and the level of IFRS compliance has also revealed conflicting results in Africa. For example, Appiah *et al.*, [32] sampled 49 listed companies and the study revealed that profitability had a significant positive effect on the accounting disclosures. However, Samaha and Stapleton [58] in Egypt, Tauringana and Chithambo [33] in Malawi, Tsegba *et al.*, [30] in Nigeria, Appiah *et al.*, [32], and Agyei-Mensah [82] in Ghana did not find an association between profitability and compliance with IFRS disclosures.

4. Hypotheses Development

4.1. Audit Quality

Audit quality is measured using various proxies both input based and out-put based, which should depend on the research setting [4]. Khlif and Achek [7] postulate that audit quality, as proxied by auditor type, may play a significant role in enforcing the compliance with IFRS. Alsaed [85] Categorized external auditing firms into two types, big 4 (Larger) and non- big 4 (smaller). Street and Gray [84] noted that large international audit firms ensure that they do not sign their names on any annual report not in compliance with IFRS as a result of pressure from the World Bank. High quality auditors issue greater assurance or opinion that the financial statements faithfully reflect the firm's underlying economics over the period under review [4]. Therefore, it is expected that firms being audited by the larger audit firm will have a higher compliance with IFRS disclosure requirements. Large audit firm also have superior training of their employees and economies of scale in terms of competence and offer more expertise than local auditing firms [86]. Contrary, smaller auditing firms are sensitive to the client's demands for fear of losing the client and income because they depend on one or a few clients [87, 88].

Several empirical studies reviewed have indicated a positive relationship between compliance with IFRS disclosure and type of audit firm. Samaha and Stapleton [58] revealed that being audited by an international audit firm is a principal cause for IFRS compliance. Hodgdon *et al.*, [89] found that compliance is positively related to auditor choice. Bepari *et al.*, [34] Found audit type (quality) are significant determinants of firms' compliance with IFRS. Al-Akra *et al.*, [68] Showed that auditor size exert a significant positive effect on IFRS compliance.

Audit quality communicates the auditor's assurance that the financial statements comply with accounting standards and denotes to the quality of the auditor's opinion [4]. However, Zambian listed companies received unqualified audit opinion despite significant non-compliance with IFRS disclosure requirements [17]. Therefore, this situation may be due to lack of audit quality because external auditors of listed companies

sit on ZICA council who is the financial reporting regulator in Zambia. This present a potential conflict of interest which can impair audit quality and lead to low IFRS compliance in Zambia. Therefore, the study hypothesized that:

H1: There is a negative relationship between listed companies audited by audit firm with partners who sit on ZICA council and compliance with IFRS disclosure requirements.

Furthermore, it is hypothesized that:

H2: Audit quality moderate the relationship between firm characteristics and compliance with IFRS disclosure requirements.

4.2. Foreign Investors

Although foreign investors are expected to demand higher compliance levels with IFRS and effectively monitor management's compliance with disclosure standards, if their shareholding is minor; they may not have the power or urgency to demand such claims [40, 46]. Almaqtari *et al.*, [76] found a statistically significant negative influence of foreign ownership on the level of IFRS compliance. However, [19, 10, 75, 31, 74] found that foreign investor is positively related to IFRS compliance disclosure requirements and the greater the foreign ownership the more the IFRS compliance. Therefore, it is hypothesized that:

H3: There is a relationship between the proportion of foreign shareholding to total shareholding and the level of compliance with IFRS disclosure requirements.

4.3. Institutional Shareholding

Institutional investors have a significant ownership stake in companies and shareholders with large shareholdings have both power and legitimacy as well as the urgency to demand compliance with IFRSs [40, 47]. However, the empirical evidence on the relationship between IFRS compliance and institutional shareholding is mixed. For instance, some studies found a positive relationship between institutional ownership and the level of IFRS compliance [82, 77]. Meanwhile, others found that ownership dispersion is negatively associated with the degree of compliance with IFRSs [68]. Juhmani [80] found that blockholder ownership, managerial ownership, and government ownership are not associated with IFRS compliance. From the literature reviewed above, the study hypothesized that:

H4: There is a relationship between the proportion of institutional shareholding to total shareholding and the level of compliance with IFRS disclosure requirements.

4.4. Firm Size

Larger firms are expected to adhere more to IFRS compliance than smaller firms due to reduced cost derived from economies of scale and to avoid political costs [12, 90, 85 and 54]. However, the extant empirical studies on the relationship between IFRS disclosure requirements and firm size have produced varied results. Some empirical studies have shown a positive association between IFRS compliance and firm size [12, 58, 11, 59, 31, 29, 78, 27]. On the other hand,

Karim and Ahmed [60] found a negative relationship between IFRS disclosure and firm size. Moreover, other studies found no association between IFRS disclosure and firm size [30, 83, 61, and 16]. Therefore, the study hypothesized that:

H5: There is a relationship between the firm size and the level of IFRS compliance disclosure requirements.

4.5. Firm Profitability

It is expected that managers are more likely to adhere to IFRS compliance when profitability is high to signal their excellent stewardship, increase investors' confidence and justify compensation [66, 67]. However, the results on the association between IFRS compliance and profitability are varied. Some extant empirical evidence shows a negative association between IFRS compliance and profitability [12, 58, 59]. Meanwhile, other studies show a positive relationship between IFRS compliance and profitability [68, 11 and 34]. Therefore, it is hypothesized that:

H6: There is a relationship between the firm profitability and level of IFRS compliance disclosure requirements.

5. Research Methods

5.1. Sampling

The population consisted of companies listed on the Lusaka Securities Exchange beginning or before 1st January 2012 and are still trading on the exchange as of 31st December 2018. The effective date of 1st January 2012 was chosen because it follows the adoption of three-tier in the financial reporting framework in Zambia. The year 2018 was selected as the end study period because it was the most recent period for which annual reports and audited financial statements of the listed companies were available, at the time of conducting the empirical work. Similar argument have been used by other prior studies [40]. Using this criterion only 20 listed companies were included in the population. It is a requirement by LuSE and ZICA that all listed companies should comply with IFRS disclosure requirements. The study employed the purposive sampling where the entire listed companies were sampled because the population was small [91].

5.2. Data Collection

The study analyzed the relationship between the firm characteristics and IFRS compliance by focusing on the moderating effect of audit quality. IFRS compliance level was used as the dependent variable and the firm characteristics which included audit quality, foreign investors, institutional shareholding, firm size and firm profitability as independent

variables. The main data source was from the annual reports of listed companies and ZICA. All the annual reports for listed companies were collected from LuSE and also some downloaded from the respective companies' websites. The annual reports for ZICA were obtained from the institute. The study employed quantitative content analysis to collect the secondary data from the annual reports.

5.3. Measuring Dependent Variables

There are two prominent methods of measuring IFRS Compliance, dichotomous disclosure index approach, and partial compliance unweighted approach [92]. The present study employed both methods as this provides more robust results that are informative compared to just a single method [92, 75].

The dichotomous method requires that the disclosure index for each company is calculated as the ratio of the total items disclosed to the maximum possible score applicable for that company. The formula is given in *equation 1*:

$$C_j = \frac{T = \sum_{i=1}^n di}{M = \sum_{i=1}^n di} \quad (1)$$

Where C_j is the total compliance score for each company and $0 \leq C_j \leq 1$. T is the total number of items disclosed (di) by company j and M is the maximum number of applicable disclosure items for company j that could have been disclosed. If a required item is disclosed, it is scored as 1 and if it is not disclosed, it is scored as 0. However, some items may not apply to every company and are therefore scored as "not applicable".

The partial compliance unweighted approach (PC method) gives unequal weighting to the disclosure items in different accounting standard as given by the formula in *equation 2*:

$$PC_j = \frac{\sum_{i=1}^n Xi}{R_j} \quad (2)$$

Where PC_j is the total compliance score for each company and $0 \leq PC_j \leq 1$. X_i is the level of compliance with each standard's mandatory disclosure requirements. Firstly, we will calculate the compliance with each standard separately, and subsequently, the sum of the compliance scores (X) is divided by the total number of relevant/applicable standards for each company j , i.e. R_j .

The dichotomous method has been adopted as the primary because it is the most widely used method based on prior literature and PC method as a robustness analysis [92, 15].

5.4. Measuring the Independent Variables

The firm characteristics were operationalized as given in *Table 1* below:

Table 1. Operationalization of the Independent Variables (Firm Characteristics).

Variables	Proxy Description
Audit Quality (Aud)	Indicator variable coded 1 for clients of auditing firms with partners who sit on ZICA council; 0 for others [34, 84].
Foreign Investors (FI)	Ratio of foreign ownership to total shareholding [19].
Institutional Shareholding (IS)	Ratio of institutional investors to total shareholding [51, 77, 50]
Firm Size (FS)	Measured as a natural Log of total assets [12, 16, 76]
Firm Profitability (FP)	Measured by the ratio profit after tax to equity [68, 19]

The frequency was used to describe the distribution of audit quality. Out of the 140 firm observations 77 represent clients of auditing firms with partners who sit on ZICA council. The range for foreign investors' shareholding was from 0.05 to 1 with a mean of 0.70 and a median of 0.75. This implies that some firms were wholly (100%) owned by foreign investors with the least foreign ownership being 5% and average 70%. The institutional shareholding ranged from 0 to 0.889 with a mean of 0.17 and a median of 0.12. This implies that some firms did not have institutional shareholders and the maximum institutional shareholding was 88.9% with the average of 17% ownership. The firm size ranged from K11.57 million to K280,674 million with a mean of K11, 053 million and a median of K1,735 million. The firm profitability ratio ranged from -5.5 to 4.43 with a mean of 0.11 and a median of 0.13. There were variations in the independent variables as indicated in the respective standard deviations. The greatest variation was in firm size with the mean considerably larger than the median signifying that the distribution is positively skewed and non-normally distributed [93]. The transformation of firm size using natural logarithm mainly corrected the non-normal distribution.

6.3. Regression Results

The study involved panel data analysis as it was a longitudinal study over a period of seven years across listed companies. Therefore, a Hausman test was done to choose between fixed or random effect model estimators to run the regression analysis. The Hausman test results indicate a P-value of 0.2622 inferring that to examine the association between the dependent variable and independent variables,

the random effect model is suitable.

Table 4 present hypotheses results regarding the relationship between the firm characteristics and IFRS compliance. The study also analysed if audit quality moderate the association between firm characteristics and IFRS compliance. The results are provided in Table 5 below. The summary of the hypotheses testing results are presented in Table 6.

Table 4. Regression Results- DI.

Dependent Variable: IFRS Compliance (DI)				
Independent Variable: Firm Characteristics				
Variable	Predicted Sign	Coefficient	z	P-Value
Auditor on ZICA council (Aud)	-	-0.040	-0.54	0.590
Foreign Shareholding (FI)	?	0.043	1.08	0.278
Institutional Shareholding (IS)	?	0.030	1.02	0.308
Firm Size (FS)	?	0.012	5.22	0.000*
Firm Profitability (FP)	?	-0.005	-2.26	0.024*
Intercept		0.350	5.95	0.000*

R-sq within = 0.2803 Wald chi2 (4) = 42.23 P-value > chi2 = 0.000

between= 0.0325 N= 140

Overall=0.0548

*5% Significance level

Table 5. Moderation Results Using Pairwise Correlation.

Firm Characteristics	Without Audit Partner on ZICA Council (AUD 0)	With Audit Partner on ZICA Council (AUD 1)
Foreign Shareholding (FI)	0.4430	0.0781
Significance level	0.0003*	0.4994
Institutional Shareholding (IS)	-0.3073	0.2081
Significance level	0.0143*	0.0694**
Firm Size (FS)	-0.0145	0.3646
Significance level	0.9103	0.0011*
Firm Profitability (FP)	-0.0187	0.0273
Significance level	0.8843	0.8138

*5% significance level; **10% significance level

Table 6. Hypothesis Testing Results.

Hypothesis	Result	Decision
H1: There is a negative relationship between listed companies audited by audit firm with partners who sit on ZICA council and compliance with IFRS disclosure requirements.	Insignificant	Reject
H2: Audit quality moderate the relationship between firm characteristics and compliance with IFRS disclosure requirements	Significant	Accept
H3: There is a relationship between the proportion of foreign shareholding to total shareholding and the level of compliance with IFRS disclosure requirements.	Insignificant	Reject
H4: There is a relationship between the proportion of institutional shareholding to total shareholding and the level of compliance with IFRS disclosure requirements.	Insignificant	Reject
H5: There is a relationship between the firm size and the level of IFRS compliance disclosure requirements.	Positive Significant	Accept
H6: There is a relationship between the firm profitability and the level of IFRS compliance disclosure requirements.	Negative Significant	Accept

7. Discussion

7.1. Audit Quality and IFRS Compliance

According to stakeholder salience theory definitive view, auditors have the power and legitimacy to demand for compliance with IFRSs and their claim is urgent. However, contrary to this view and H1, the results reveal that there is an insignificant relationship between the partners of audit firms of listed companies sitting on the ZICA council (audit quality) and IFRS compliance. These results suggest that

audit quality is not compromised by audit partners sitting on ZICA council. The plausible explanation is because the audit firms for listed companies in Zambia are big firms and have an international affiliation which makes them provide quality audit. This position is consistent with prior studies such as [28, 32, 69-71, 34, 58] who found a positive association between big audit firm with international affiliation and compliance with IFRSs. This is because large audit firms with international affiliation are under pressure to provide quality audits and they also have superior training of their employees and economies of scale in terms of competence and offer more expertise than local auditing [84, 84].

Moreover, smaller auditing firms are sensitive to the client's demands for fear of losing the client and income because they depend on one or a few clients [88, 87].

Furthermore, the moderation effect of audit quality reveal a significant positive association between listed companies without audit partners sitting on ZICA council with foreign ownership and compliance with IFRSs. There is also a significant negative association between listed companies without audit partners sitting on ZICA council with institutional shareholding and compliance with IFRSs. On the other hand, there is a significant positive association between large firm with audit partners sitting on ZICA council and compliance with IFRSs. These results indicate that audit quality moderates the relationship between firm characteristics and IFRS compliance. The results resonates with [72] who found that audit quality as an external governance factor mediates the relationship between internal corporate governance and IFRS convergence.

7.2. Foreign Investors and IFRS Compliance

Regarding the relationship between foreign investors and compliance with IFRSs, the results shows a positive but statistically insignificant relationship which is contrary to H1 that there is a relationship between foreign investor and IFRS compliance. This is also contrary to other prior studies such as [74, 29, 31, 75, 19, 12] who found a positive statistically significant relationship between foreign shareholding and IFRS compliance. However, the study result is consistent with [40] who observed that foreign investors in Africa are more interested in the resources of the country, not compliance with laws or accounting standards because the majority of them hold key positions thereby having access to internal information and hence no need for requesting high compliance. This view is consistent with the observation from this study that despite having a large foreign shareholding averaging 70%, there was low compliance with IFRSs among listed companies in Zambia.

7.3. Institutional Shareholding and IFRS Compliance

The H4 suppose that there is a relationship between institutional shareholding and IFRS compliance. However, the result show a statistically insignificant positive relationship between institutional shareholding and IFRS compliance. The result is also in contrast with the stakeholder salience theory which suggest that institutional shareholders are legitimate stakeholders with power and may have the urgency to demand for IFRS compliance. Further, the result is contrary to other prior studies such as Ebrahim and Fattah [77] in Egypt who found evidence that institutional ownership improves compliance with IFRS disclosure requirements. On the other hand, the result resonates with other studies such as Al-Shammeri et al., [12], Białek-Jaworska and Matusiewicz [71] who found an insignificant association between ownership structure and IFRS compliance. The reason for this result could be that the institutional investors may have little interest in IFRS

disclosures since they have access to management [48, 40].

7.4. Firm Size and IFRS Compliance

Consistent with H5 the result shows a significant positive relationship between the size of the firm and compliance with IFRS disclosures. Furthermore, the result resonates with other prior studies such as [27, 29, 31, 12, 19] who also found a significant positive relationship between firm size and IFRS compliance. This result can be attributed to the fact many stakeholders demand for improved accountability and transparency through disclosure of information especially from large companies in the extractive industries in Zambia [63]. In addition, it could be that larger firms reveal more information than smaller firms because they have a wider shareholder base and lower information processing costs [86, 90, 12].

7.5. Firm Profitability and IFRS Compliance

Agency theory conjecture managers as agents of the shareholders and are expected to reveal more detailed information if profitability is high to signal their excellent stewardship, increase investors' confidence and justify compensation [66, 67]. In contrast, the study findings reveal that there is a negative statistically significant relationship between firm profitability and IFRS compliance. Companies may be motivated to hide profits through low compliance with IFRSs to avoid being in the political limelight. However, these results are consistent with [71, 31, 27] who found negative significant relationship between profitability and IFRS compliance.

8. Conclusion, Implications and Limitations of the Study

The present study examined the association between the firm characteristics and compliance with IFRS disclosure requirements by focusing on audit quality as a moderating variable on this relationship. The study findings show conflicting results which is similar to other previous studies. The study shows a positive association between firm size and IFRS compliance. On the other hand, the results show that there is a negative significant association between firm profitability and compliance with IFRS. Lastly, there is a statistically insignificant positive association between institutional shareholding, foreign shareholding, audit quality and IFRS compliance. However, audit quality moderates the relationship between foreign ownership, institutional ownership, firm size and IFRS compliance.

According to the findings, larger company discloses more information than smaller firms because of stakeholder demand, larger shareholder diversity and lower information processing costs. Meanwhile, profitable firms fail to provide detailed information. Furthermore, Institutional investors and foreign investors do not influence IFRS compliance probably as a result of institutional investors and foreign investors in Zambian listed companies being transient investors who have

no substantial motivations to monitor company management. Audit quality perform a moderating role in influencing IFRS compliance.

The study makes contribution by considering the moderating effect of audit quality on the association between firm characteristics and IFRS compliance. In addition, the study examined the influence of firm characteristics on IFRS compliance in Zambia and hence, makes a contribution to similar studies examining the antecedents of IFRS compliance focusing on a developing country in Africa of which the research is insufficient and conflicting evidence [27, 32, 59, 70, 19, 33, 68, 11, 58, 12].

The financial reporting regulators should focus on enhancing audit quality for listed companies in Zambia. The study shows that large firms are more likely to adhere to IFRSs. Therefore, the financial reporting regulators should come up with a deliberate plan to guide small firms with the interpretation and implementation of IFRSs. Besides, more research can focus on the relevance of IFRS disclosures to the domestic investors in Africa considering the cultural differences both at firm and national-level.

Generalizing the findings from this study to other developing capital markets in Africa should be done with caution due to differences in the institutional settings.

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