"The Prospects of Accounting in Kuwait"

The Accounting Department
Kuwait University
Kuwait, 1993

The paper also investigates difficulties in setting accounting standards in a developing country: Kuwait.

An understanding of the development of accounting and regulation in Kuwait will be necessary to its advancement. The countries in the region, as well as those of the developing world, must be aware of the need to safeguard accounting standards and procedures. A number of proposals have been put forward for the regulation of the accounting profession in the country: first, an authoritative body to hold the responsibility of enforcing standards of practice; second, a conceptual framework for adopting a specific standard or code; third, greater communication with all concerned parties.

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Synopsis

The paper aims to investigate difficulties in setting accounting standards in a developing country; Kuwait.

An understanding of the prevailing problems of accounting regulation in Kuwait will be conducive to its improvement, not only for the case of Kuwait, but also for neighbouring and developing countries in general. The current change in the region offers a golden opportunity to work for and secure a solid accounting profession regulation.

A number of proposals have been put forward in this paper that may contribute to the regulation of the accounting profession in the country: first, an authoritative body to hold the responsibility of securing standards of practice; second, a conceptual framework for adopting a specific standard or code; third, greater communication with all concerned parties.
Introduction

This paper aims to investigate difficulties in setting accounting standards in Kuwait as concluded from the work of the Permanent Task Committee - PTC (or the Committee for the Establishment of Accounting Rules - CEAR). The examination of the PTC's work will enlighten concerned parties about the problems as well as the type of accounting regulation most appropriate to Kuwait, and provide a framework for the regulation of the profession.

An understanding of the prevailing problems of accounting regulation in Kuwait will be conducive to its improvement. This task is of grave importance not only for the accounting profession, but also for similar professions to be constituted.

First, a brief examination is made of the origin of accounting in the country, including the establishment of the PTC. The performance of the PTC is evaluated in the second section. The third section is a presentation of a general model to accommodate the new structure of regulation in Kuwait. Finally, recommendations for regulation are made in the concluding section of the paper.
I. Roots of Accounting Regulation in Kuwait

Kuwait has known accounting since 1940 as a consequence of the economic expansion in the area. Accounting began as a book-keeping and recording liability function, and such regulations as existed at that time were imported from neighbouring and other Arab countries.

The need for accounting as a financial reporting function has become more acute in recent years, particularly since the AL-Manakh market collapse in summer 1982, which prompted private investors to turn to accounting to provide informative, reliable, and timely financial reports to avoid another crisis.

This issue has also been taken up by the government, resulting in further supervision of accounting firms.

"Lately, following the AL-Manakh crisis, the accounting firms have been subjected to some supervision from the government. However, they remain themselves largely responsible for the standard of auditing and the quality of their work." (1)

The need for accounting standards is one widely accepted nationally. They already fill volumes, and are proliferating to keep pace with the growth in international trade and the development of international capital markets, as well as to obtain greater harmonisation in the preparation of financial statements.

Efforts made to regulate the profession in Kuwait have taught us that certain conditions have to be present for the effective introduction of accounting standards. The process of issuing standards has now acquired momentum, and aroused such high
expectations that it is accepted as irreversible. Likewise, the study of standards now plays a great part in most accounting curricula, underlining the profound influence standards have on the future of the accounting literature.

The Establishment of The PTC

The absence of an active accounting body forced the government to bear full responsibility for regulating the practice of accounting and auditing. Thus, the task was entirely left to the discretion of the ministry of Commerce & Industry. Sadly, confidence and trust in the profession's ability to lead the regulatory process was somewhat lacking.

"The profession's failure to establish accounting and auditing standards as well as rules of conduct, had led the government to provide rules and standards in addition to the needed reporting disclosure regulations". (2)

However, the government's achievements in this period were insufficient to meet the need for advancement of the local profession. Some writers have gone so far as to state that it was the accountants' dissatisfaction with the government role, which led to the establishment of the Kuwait Society of Accountants and Auditors (KSAA) in 1973. (3)

There was general agreement on the need to improve the structure of accounting practice. This need was reflected in the establishment in 1981 of the Permanent Task Committee (PTC), formed by the Ministry of Commerce & Industry. The purpose of this
committee was to improve accounting practice locally as well as to
set the required accounting rules. (4) Indeed, this development was
first and foremost, a significant indication of the government's
desire to improve the accounting system.

"While it was possible for the government to enact
new regulations on its own without consulting the
profession as was the case in 1962, it was obvious
that the government was seeking improvement in
accounting practices rather than just adding more
regulations. [another change]... was the mutual
understanding between the government and the
profession that public accounting practices had matured
enough to surpass the era of loose regulations." (5)

The PTC was formed of 5 representatives, 3 from the Ministry
of Commerce and the other two from KSAA and Kuwait University. Its
objectives were:

1. To develop a code of ethics;
2. To set standardised financial reporting rules;
3. To establish minimum disclosure requirements;
4. To review periodically existing rules and accounting procedures;
5. To research and study means of improvement.

The PTC did not really become active until 4 years after its
establishment, when it issued 3 accounting guides. These guides
were: 1) Financial data disclosure, 2) Accounting for Investments,
3) Estate Accounting. However, the PTC was adversely affected by
government routine and the ineffective planning measures of its
meetings.

"The CEAR (PTC) has been charged with
responsibilities beyond the capability of its
members. The majority of its members lack the
needed knowledge and experience to achieve the
desired goals." (6)
II. Problems Facing The PTC

Although the PTC had the motivation and the reasonable government backing, it encompassed several shortcomings. The PTC's guides were not based on clear assumptions which could have enhanced their credibility and supported their pronouncement. For example, the Solomons report in Britain was partly based on the comparability assumption, "Good accounting standards make like things look alike". (7)

In addition, PTC issues would have been better received had they confined themselves to specific statements determining the recommended procedure, rather than allocating many pages for describing forms of procedures and classification of types of assets or liabilities. Discussion of this sort should be kept as brief as possible.

Over all, the PTC's major obstacles are discussed according to their importance below.

Adherence

The PTC is a state-regulating body, constituted of assigned members which in ten years managed to issue only 4 accounting guides. However, adherence to these guides by users and preparers of accounts, which would be a vital component committee's success, has not been achieved. The current volume of accounting guides issued by PTC does contain a number of extant treatments, but the main theme of standardising accounting practice represents a confession of failure.
It seems that the PTC's central problem is lack of authority, as the enforcement of the guidelines is weak. To this criticism, some would like to add a lack of direction. The PTC, because of its weak powers, has had to take a consensus view and has frequently made concessions to placate influential financial users. Evidence of this deficiency is observed in the top secrecy that has surrounded the work of PTC, and the silence of the PTC regarding vital issues in Kuwait, such as the take-over attempts and consolidations of companies.

Concepts

More fundamentally, the PTC has tended to lack a consistent set of central concepts which would lend coherence and consistency to the set of standards as a whole. An obvious example of this problem is the issue of valuation. The PTC has not adopted a method of valuation nor has it provided a conceptual framework for such valuation.

Another dimension of this problem is the incompetent pronouncement of general principles derived from the conceptual framework. The issued guidelines were not detailed enough to be considered as standards of practice in order to achieve a true and fair view. Standards should indicate certain practices by which measurements are made and economic outcome reported, not merely specify forms of reporting. In other words, it is an issue of substance over form.
standards setting as well as guidelines for reporting, or what is popularly known as a conceptual framework. The Committee should investigate not only the soundness and reasoning of reports, but also whether they point in the appropriate direction for practical development. Standards could, for example, be based on a description of a problem to be investigated, a logical discussion of possible solutions, and a prescribed solution.

Support

It could be due to the lack of professional support and discipline that the enforcement problem arises. Accountants are appointed by directors who prepare accounts in the first place, and few of them report any departure from the PTC's guidelines as long as reports represent true and fair view.

"The Auditor is merely required to report departure from accounting standards (and then only if the departure is not deemed to be justified by, for example, the over-riding need to present a true and fair view), not to correct the departure." (8)

There is evidence that listed companies are not following the issued guidelines. (9) The examination of the published financial statements indicate little, if any, adherence to the guidelines.

Moreover, the PTC's work has lacked support from the public at large. This phenomenon is, however, by no means unique to the PTC, or to Kuwait. In the U.K., for instance, the support for accounting standards which would better reflect changing money values in financial statements has steadily declined as inflation itself has declined and with it public interest in the matter. "Ultimately it is the users of accounting information, not accountants, whose
approval of accounting standards is important". (10) After all, it is the business community and the public at large by whom standards are to be observed. Obviously, managers prefer flexibility rather than to be bound by rules. For this reason, as sadly concluded by Professor Moontiz, "a professional body, acting by itself, is incapable of obtaining agreement on a set of accounting standards. the layman simply will not let it do the job". (11)

In fact, users of financial statements do not place a high value on what they perceive to be unreliable information, especially where the lack of adequate accounting means "that in many cases management has too great influence on the form and content of financial statements which are often regarded as reports by management rather than reports on management". (12)

**Pressure**

The PTC has to accommodate pressure sources, particularly; the structure of the accounting profession in Kuwait, state dominance, and other groups' interests. In getting from an assumption to a standard, normative judgement had to be made about what kind of accounting is desirable and for whom ?.

The accounting profession's structure - in other words, the structure of auditing firms - puts limits on the PTC's freedom to issue preliminary exposure drafts of proposed standards. Also, the extensive range of auditing rules prescribed by these firms to arrive at a fair and true view, offers little opportunity for reconciliation of the Standards.
"The large scale environment requires rule books, to co-ordinate the large number of individuals involved in the team, and leading firms have devised their own large and comprehensive audit manuals, setting out their standards procedures in detail" (13)

One has also to appreciate the increasing international pressure on regional bodies to set accounting standards (European Community stress on uniform accounting, the pressure to confirm with US practice by FASB and SEC, and the strong effect IAS have on developing nations). (14)

Indeed, there have been calls for the adoption of international accounting standards in Kuwait:

"Enterprises in Kuwait should consider carefully the selection of the accounting policies which best suit their business and organisation structure. Once selected, these policies should be applied on a consistent basis. Any departure from these policies should be disclosed. In fact, there should be greater compliance with IASC standards which, in our opinion, are more relevant to Kuwait than either U.K. or US standards." (15)

Of course, government intervention in the process of setting the standards or in its enforcement has a great effect the PTC, let alone the fact that the PTC was formed by the Ministry of Commerce. It can be appreciated that accounting standards-setters have to accommodate political pressure in the substance of the standards. Yet, standards should not be merely a tool for political or social ends, nor should standards-setters should bow to political pressures. (16)

It is depressing to note the widespread belief among accountants and concerned parties that the reliability of financial reports is being suspected since it is thought that the manner of
preparation reflects political bias. Certainly this will reduce the confidence of financial users in the information prepared accordingly, as it is clearly declared by Solomon:

"The purpose of accounting is to provide information that is needed by those who control economic resources to aid them in allocating those resources and in using them effectively. If that information is slanted for political ends, its value for decision-making will be reduced and the confidence that it commands will also be reduced. Stopping this erosion of confidence is a task of the highest priority for accountants." (17)

Accounting standards must be consistent with agreed objectives of financial reporting if they are to be accepted by the preparers or the users of the reports. Thus standards are viewed differently from one country to another, as the objectives of reporting differ. In this respect, political involvement in the setting of standards is not an abuse of power as long it serves the public interest. However, personal or fictional interest should not be allowed to prevail. Solomon made this point succinctly:

"If the derivation of different standards from different reporting objectives is what is meant by 'political activity', there is nothing wrong with it. It is important, however, that the objectives be defined to serve the public interest and not some sectional interest." (18)

Various standards-setting methods currently exist, where the choice of method depending on the economic and social factors of the country concerned. Yet, a glance at the guidelines published by the PTC indicate that such factors were not considered. The influence of IAS on the work of PTC is quite clear, to the extent that the wording of some of these guidelines was a translation of those of the IAS. It is, however, difficult for a standards-setting body to accommodate every demand, especially when demanding different policies.
Secrecy

Despite the great importance attached to the work of the PTC, few had access to their meetings and final reports. While in other countries, such procedures are kept open to concerned people through exposure drafts and public hearings, in Kuwait it was shrouded in secrecy. It seems that the 5 part-time members of the PTC met too seldom and had little contact with the concerned parties and the business community.

Researchers, academicians, and accountants in audit firms are denied access to a copy of the PTC meeting agendas or discussion papers. One would have to lobby for such relevant documents. The top secrecy associated with the work of the PTC accentuate the extent of pressure the PTC had to accommodate.

A Look for A Foundation

All in all, one could summarise the problems of PTC as follows:

1) Lack of authority;

2) Lack of support by concerned bodies and accounting firms;

3) Failure to adopt a clear conceptual framework;

4) Lack of co-operation with concerned parties, as participation was not properly sought by PTC (through public hearing or exposure drafts, for example);

5) The relatively short period of time assigned for the PTC to start the setting process (i.e., the preparation of the first 3 issued guidelines took the PTC only 3 months, including all formal procedures);

6) Lack of action to enforce the guidelines.
Despite all the problems the PTC has encountered, the committee itself was considered a step in the right direction. Its effectiveness will, however, depend upon the commitment of the bodies concerned and their compliance with its rules and guidelines.

It is time for the accounting profession to establish a solid foundation for itself. As early as the 1970's, calls were made for the quick organisation of the profession:

"...It is at this stage that the accounting profession has a tremendous opportunity to help speed the process and to establish itself in society as the protector of the public interest."

"...To be effective, professional accounting groups must be better organised and be more concerned with the identification and standardisation of accounting practices... The accounting profession [also] should establish an acceptable list of accounting principles and auditing procedures in the country." (19)

These standards are the foundation of a true profession:

"Accounting and auditing standards are a requirement for the development of a financial accounting profession; these standards are necessary for determining the appropriateness of accounting and reporting practices. Accounting and auditing standards are the foundations of the practice of the accounting profession; hence, they should be the initial concern of a professional organisation in a developing country." (20)

There is a widespread tendency toward regulating the accounting practice in the country. The aforementioned problems accentuate the need for a thorough evaluation process of accounting regulation in Kuwait.

An alternative is to establish a framework for structuring the profession on a conceptual basis, which is the main purpose of this
III. Accounting Regulation Model

As evidence of the division of opinion that exists among concerned persons about the technical aspects of accounting regulation in the country, it is instructive to look at the poll conducted by the writer in 1990.

An opinion form was circulated among a cross-section of those with a special interest in this matter. The total number of respondents was 31, most of whom (17) were accountants in audit firms. The remaining participants were academicians (7), members of the PTC committee (2), officials of the ministry of commerce (2), representatives of Kuwait Society of Accountants (2), and one respondent from the Audit Bureau. The objective of the opinion form was to examine initial views concerning the role of the government and other parties in the regulation of the profession. A summary of the poll results is given below:

1> 90% of respondents were not much in favour of the government management of the regulation process, although they admit the importance of government adoption and support of the standards issued. They hold that state interference in the technical side of accounting should be kept to a minimum. The role of the ministry of commerce is better limited to the administrative and legal part of the process rather than the process of discussing and then issuing standards of practice.

2> 34% believed the public are not concerned with the regulation process nor its effect on financial reporting. They made
distinction between business educated, and ordinary persons. The
business oriented people are most likely to be involved or affected
by the regulation progress. Such individuals should be consulted at
the first stages of guidance issuance, especially as they form a
relatively small percentage among the population (25-30%) but exert
considerable influence on the regulation process.

3> 57% considered responsibility for regulation as a matter of
degree or a combination of private and public inputs, though they
placed great emphasis on the private sector role in regulation of
the profession.

4> Respondents were undecided whether standards ought to be
binding rules or be followed on voluntary basis. Yet, a
considerable percentage (79%) of them believed that there should be
a basic level of compliance by practitioners, enforced by an
executive party with the right to apply certain penalties and
rewards.

5> All respondents agreed on the desirability of establishing an
independent accounting body charged with the responsibility of
setting accounting standards, observing adherence to these
standards, and regulating the profession in general.

6> All respondents demanded the adoption of a follow-up system
aiming at monitoring the progress of the regulation process and its
effects on the profession, and the financial sector in general.

For a PTC type body, a systematic approach should be
accounting regulation in Kuwait:

1. Is there a real need for accounting regulation?

2. Should such regulation be carried out in the public sector rather than the private sector?

3. Is self-regulation by the accounting profession considered? And what are its chances of success?

4. Is accounting standards enforcement of paramount importance in Kuwait?

5. How should accounting standards be enforced (what form should standards take)?

6. Is it necessary to establish an independent accounting standards authoritative body? And what form should it take?

7. Should an evaluation framework of accounting standards setting be adopted?

It is important to consider these questions cohesively, as they clearly spell the most suitable approach for setting standards. If the answer to the first 3 questions (above) is positive, then the matter will be left to the professional body charged with the regulation process.

Although the experiences of others ought to be considered, the work of the emerging regulatory body must not blindly copy other countries' undertakings in setting accounting standards.
A Professional Body

The model is based on the establishment of an authoritative agency assigned the task of setting the standards. The authority is state-oriented in terms of formation and regulation, but independent in terms of setting the standards. The authority will be the centre of the setting process, where all concerned parties participate in the sub-committees formed through the authority (figure 1). If accountants participate in the work of the standard-setting agency, they are more ready to accept the standards produced, even if these do not conform to their own personal views.

In order to enforce the standards and guidelines, the authority should be attached to a government agency or ministry. This will give the authority the assurance of full adherence and co-operation by accounting bodies as well as accountants. Likewise, departments or divisions could be established for each profession under regulation.
Ministry of Commerce

ACCOUNTING REGULATION AUTHORITY

International

Other Parties

KSAA

Accounting Firms

End User

Departments could be established for other professions (e.g., Economists, Financial Analysts).

The Proposed Status of Accounting Regulation

An independent authoritative body. State Authority in terms of regulation and power, but keep as original in terms of formation, setting standards, and follow-up.)
However, this by no means indicates that the responsibility of the government or the suggested authority is complete. The input of the accounting profession (mainly KSAA, the accounting firms) is vital and should be based on active participation, not on adherence only. The private sector should also be involved in the continuous process of follow-up and review of what are expected to be mandatory requirements as far as they are concerned. "This is particularly relevant when professional accounting bodies prove to be more active and capable of assuming responsibilities in that direction". (21)

One of the hallmarks of a professional society is that its members accept standards of behaviour and performance above the law. It is in this way that they demonstrate the right to continue to hold the public trust and confidence, which is necessary for a self-regulated body. It is a matter of securing credibility of financial reporting in the eyes of the public:

" How do you explain to an intelligent public that it is possible for two companies in the same industry to follow entirely different accounting principles and both get a true and fair audit report? The public might want to know how many true and fair views ... and whether there is any common standard against which to measure them all." (22)

The public, and the business community in particular may find it difficult to adopt the revolutionary reform of the accounting requirements. This will also require an industrious effort on the part of the accounting authority to educate them.

Accountants & Auditors

It is not only the preparers and the users who require such
may not be willing or able to comply with the new arrangements and the discipline imposed by the accounting standards. In most cases, "They (the accountants) are content to apply their own interpretation and not necessarily a consistent one, of what constitutes minimum compliance with the law - where such law exists." (23) It is, therefore, exceedingly important that there exist an active certified professional society that can persuade its members, the leaders of the profession, to accept not only the substance of the accounting standards but also their spirit and intent.

Obviously, the time has to come to impose certain sanctions against those who do not fully comply with the obligatory standards. The profession, in this regard must have the machinery to discipline those of its members whose standards of conduct fall below that which is acceptable and likely to bring the profession into disrepute. In addition to any legal action which might arise, the authoritative body should have the power, through the proper channels, to withdraw licences from persistent offenders.

The Framework

Whatever the approach selected by the authoritative body, its value will depend on the practicality of the standards issued. The usefulness of the final product is more important than the manner of production. According to Storey, "accounting principles developed in essentially the same manner as the common law, on a case-by-case basis, and the ultimate test of their acceptability was their utility." (24)
The importance of a conceptual framework for standards-setting comes from the fact that it would eliminate most of the conflicts arising from undisciplined development of standards, as such a framework would determine the basis on which priorities of financial statements production would be built. The English Institute of Chartered Accountants has said:

"Indeed without the framework, the development of some SSAP's may be delayed, or prove contentious than might otherwise be the case". (25)

Similarly, the accounting standards review committee of the Scottish Institute said:

"It is imperative that work work begin immediately on a conceptual framework rather than that the present practice of producing standards with no theoretical underpinning should continue". (26)

The components of such a framework will certainly depend on the perceptions and objectives of the body assigned the task of setting the standards. Yet, the framework must not be utilised only to answer questions concerning the usefulness of the standards and for whom. Questions such as the communication of the reports, quantity, timing of disclosure, and the prime users of the reports would be considered by the body in achieving its task. Solomons, in evaluating the attempt of the FASB to construct a conceptual model said:

"These are important questions which will be covered by the FASB's projects; but they raise less fundamental issues than the main components, and any answers that are given to the subsidiary questions are likely to need revision and updating". (27)

He further introduces five main fundamental components of the emerging model, which are:

1) A statement of financial reporting objectives;
2) A set of financial reports definitions;
3) Characteristics of financial statements;
4) Criteria for deciding when to recognise the elements of financial statements;
5) A set of measurement rules. (28)

In any event, regardless of the orientation of the adopted framework, it should be concentrated on two main themes. The first is the suitability of the framework for the local environment (social, political, economical, etc.) of Kuwait; the second, the practicality of the framework to facilitate the complicated task of the body charged with regulating the profession.

"A standard is a rule to be followed so long as it fits the facts. The accountant should be free - and is indeed obliged by the 'true and fair view'- to depart from it when he judges that it will distorts the picture. (29)

Practicality would entail the restriction of government routine and bureaucratic procedures, while at the same time building the fundamental elements on solid basis. The argument here, is to explicate both the theoretical foundation, and the multiple procedures required to issue standards. Any deviation from standards ought to be justified, described and estimated in terms of its possible numerical effect.
IV. Conclusion

What is the future of accounting profession organisation in the country? The answer may well ultimately rest with the foresight of the government. Yet, a great dependence is now laid on the aspiration and efforts of the accountants and their representative bodies.

The current period of change and reconstruction in the country, and indeed in the region as a whole, offers a golden opportunity for accountants to work for and secure the regulation of the profession. For example, repatriation claims and the government attitudes toward rectifying the migrant percentages (which will create more demand and more chances for Kuwaiti college graduates to be recruited within the profession), are significant vindicates for the efforts of the accounting bodies in this respect. With the support of the government and the encouragement of the profession, one would hope that an accounting authoritative body, as well as standards and codes of ethics, would soon emerge.

A number of proposals have been put forward in this paper that may contribute to the regulation of the accounting profession in the country: first, an authoritative body to hold the responsibility of securing standards of practice; second a conceptual framework for adopting a specific standard or code; third, greater communication with all concerned parties, including the business community, the accounting firms, the international accounting platforms, and the
public in general; last but not least, action by the government, represented by the Ministry of Commerce, to establish an organised accounting profession.

However, it would be naive to expect that the majority of contentious issues will be resolved because accounting standards are in existence. The grey area may be narrowed but it certainly will not be eliminated. There will still be many circumstances where different interpretations will be placed on the application of standards and further guidance will be required.
NOTES

1. Accounting Practice in The GCC, Deloitte Haskins + Sells, Middle East Economic Digest Ltd., 1984, p. 43.


3. Ibid., P. 90.


6. Ibid., P. 306.


14. Ibid.


18. Ibid., p. 113.


27. Solomons D., "The Political Implications of Accounting and Accounting Standards Setting"; op. cit. p. 112.

28. Ibid. p. 111.

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