Determinants of Internet Financial Reporting: An Empirical Investigation on UAE Public Listed Companies.

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ABSTRACT

The main purpose of this study is to provide insights into the use of internet for disseminating financial information among UAE publicly listed companies and to put some lights on the factors that affect such companies in adopting financial disclosure through internet. The findings show that UAE companies are still to some extent placed behind those in other developed countries and even with other developing countries. This study additionally examined the effect of three factors namely firm size, leverage and profitability on internet financial reporting (IFR). A linear regression analysis is applied for this purpose. Findings reveal that profitability and leverage do not significantly influenced internet financial reporting. The result also shows that there is a significant positive linkage between the amount of financial disclosure through internet and size of companies.

DEDECATION

My lovely great beloved Mr. Bashar Almansour

DECLARATION

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AMMAR YASER MANSOUR AL-MANSOUR

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TABLE OF CONTENTS

CHAPTER THREE: METHODOLOGY

LIST OF FIGURES

LIST OF TABLES

LIST OF ABBREVIATIONS

Compound Annual Growth Rate	CAGR
Chief Executive Officer	CEO
Electronic Data Gathering, Analysis and Retrieval	EDGAR
Efficient Capital Market	ECM
Extensible Business Reporting Language	XBRL
Security and Exchange Commission's	SEC
Foreign Direct Investment	FDI
Internet Financial Reporting	IFR
Investment Management and Research	AIMR
National Bank of Abu Dhabi	NBAD
United Arab Emirates	UAE

CHAPTER ONE

BACKGROUND

1.0 Introduction

The forces that give rise in demand of information disclosure in modern capital market stems from the information asymmetry and agency conflicts that exist between management and stockholders. The solution therefore to agency conflicts lies in the ownership structure and the function of board of directors.

Jensen and Meckling (1976) find that ownership structure is assessed by the proportion of shares held by managers and blockholders. Managerial ownership which is the proportion of shares held by the chief executive officer (CEO) and executive directors, and blockholder ownership (which is the proportion of ordinary shares held by substantial shareholders) are two major governance mechanisms that help control agency problem. In addition, Fama (1980) argues that the board of directors is the central internal control mechanism for monitoring managers.

Financial reporting and disclosure are important resources for management to communicate firms' performance and success of efficient capital market (ECM). Fama (1991) defines ECM as a market in which new information is accurately and quickly reflected in share prices.

Firms provide disclosure by financial statements, management discussion and analysis, and footnotes. Some firms are involved in voluntary supply such as internet sites, press releases, conference calls, management forecasts.

Nowadays many companies provide their financial information on the internet since the increasing use of the internet as a medium for corporate information. The companies can voluntarily disseminate large quantity of both financial and non financial information to various groups of users which they can easily access, through their corporate servers. Internet Financial Reporting (IFR) gives the companies opportunities with more flexibility of the type of information disclosed and the presentation format of disclosures as a comparison with the traditional paper – based disclosures. IFR may consist of annual reports, stock price, data, analyst reports, press releases, and management discussions of operations. The content of the presentation formats used in IFR are hyperlinks, dynamic graphics, processable file formats, and video/audio files (Kelton and Yang, 2005).

The internet gives companies much more options than print form including plenty of space to add financial pages and even audio and video clips (Koreto, 1997) and interactive information dissemination is not possible in print form in a fashion that is achievable in the web (Lymer et al, 1999).

Web–based reports may reach a wider audience because of its powerful tool to disseminate financial reporting. Therefore, analysts, users, and investors have many options about which internet financial disclosures to view. Moreover, the incentive to

voluntarily reveal information is still under interest to both analytical and the empirical researchers. Analytical research concerned and verified issues as how competition affects disclosure, (Darrough and Stoughton 1990). Empirical researchers documented the influence of firm characteristics like size, leverage, listing and managerial ownership on disclosure.

The rising importance of disseminating financial reporting using the internet has attracted many researchers from different countries. However, most of these studies concentrate on developed countries by examining potential factors that influence the extent of internet financial reporting (see for example Gray and Depreceny, 1997; Ashbaug et al, 1999; Marston, 2003; and Oyelere et al, 2003). The extent of financial information disclosed via the internet in these countries has increased over the years. Studies in developing countries indicate that IFR among developing countries is still behind those of developed countries (Ismail and Tayib, 2000).

In the context of United Arab Emirates (UAE) companies very scant investigations have been carried out in this area. This study therefore attempts to identify the factors that influence the UEA companies to disclose their financial information via internet. Additionally, it attempts to investigate the status of IFR among UAE listed companies.

1.1 Overview of Economic in UAE

UAE is the second largest economy after Saudi Arabia in the Gulf Cooperation Council (GCC) and is one of the most open and integrated economies in the region. UAE's growth momentum continued in 2007 (moderated in comparison to 2006 due to lower oil production mainly because of UAE's commitment to OPEC) with the economy posting its fifth consecutive year of strong economic growth.

Prudent government spending at the federal and emirate levels has led to a decline in the non-oil fiscal deficit (excluding investment income) as a percentage of Growth Domestic Product (GDP)**.** At the same time, however, a number of large investment projects are being undertaken by public and quasi-public entities outside the budget in the hydrocarbon, infrastructure, real estate, and tourism sector, as a result of which government debt has increased. However as a percentage of government revenue, it is on a declining trend. Detailed strategic planning for economic growth in the coming period has also been a strong feature of financial governance during 2006-2007 with the announcement of Plan Abu Dhabi 2030 and Dubai Strategic Plan 2007-2015.

During 2007, the economy of UEA grew at a healthy pace with the nominal gross domestic product (GDP) grown by 16.5% in 2007 to reach AED698.1bn (US$190.1bn) while real GDP grew by 7.4%. Real economic growth, which excludes the direct impact of changes in oil prices, grew at a Compound Annual Growth Rate (CAGR) of 9.3% per annum in the last five years and is among the fastest rates in the

world. Construction, real estate, banking and tourism sectors have been the main drivers underpinning the real GDP growth.

However, despite the recent successes of diversification efforts of some of its emirates, oil and gas sector contributed 35.0% to the country's GDP in nominal terms in 2007 and continued to be critical for UAE's economic growth. Nonetheless, the non-oil sector had tremendously benefited from high oil prices that were in turn supporting government spending, upon which many non-oil activities depend and had grown at an impressive rate with construction, real estate, banking and tourism sectors leading the way**.**

Currently a concerted effort is made by the authorities in each Emirate to diversify its economic base so as to de-risk the economy from oil and sustain future growth. The authorities in each Emirate thus have been liberalizing their policies and encouraging both private and foreign companies to invest and become a part of the country's growth. Dubai government has taken the lead in bringing fresh investments and making the Emirate an attractive lifestyle destination in the world by freeing up the economy, developing free zones and industrial cities along with investments in huge projects such as Dubai World Central comprising what will be the world's largest airport at Jebel Ali and Dubai Logistics' City, among other facilities. All the Emirates are setting up free zones, real estate projects, industrial cities in order to attract investors and businesses. Transport and communications have reached new heights with the main seaports in Dubai and Abu Dhabi undergoing large-scale expansions and

the Dubai Metro having just completed a trial run. The strong growth in demand and increased profitability too has spurred the corporate sector to invest in new ventures or expand their existing facilities.

The efforts of the government have started to bear fruit with UAE fast emerging as an important hub for international trade, finance, and tourism. It continues to attract large inflows of foreign direct investment (FDI) and expatriate workers, and is increasingly playing an important regional economic role. According to the latest ranking in the Global Financial Center's Index - published by the City of London - Dubai is now placed among the top 10 most competitive financial centers in the world– representing the quantum jump of Dubai's status as a centre of commerce.

The real estate and construction, manufacturing, financial services and tourism sectors have also witnessed increased investment and activity. Furthermore, strong consumer confidence, underpinned by low real interest rates and rising household income and wealth, has bolstered private consumption.

The strong all round macro economic growth and high liquidity in the region on the back of high and rising oil prices and negative real interest rates was reflected in the performances of capital market as well with the National Bank of Abu Dhabi (NBAD) General index gaining 43.6% in 2007. The recovery in 2007 after the fall of 2006 was helped by the good corporate earnings growth, new listings and increased foreign investor participation.

The government's main challenges include pushing ahead with diversification into more labor intensive activities, and leverage the Emirate's strong hydrocarbon sector to stimulate and support broader economic growth**.**

The market breadth depicted the trend as collective figures of both the markets showed that there were 66 advancers and 25 decliners. Out of the total market volume of 10.4bn shares, about 88% was accounted by the advancers. With regard to primary market, Future Pipe Industries had pulled out in 2007, its IPO on the Dubai International Financial Exchange, due to conditions in the equity capital market and recent events in the financial markets. Dubai Financial Market recorded a net profit of AED 314mn from operational activities and investments for the first quarter of 2008, an increase of 231% compared to AED 95mn reported for Q1-2007. UAE markets are likely to remain in firm zone as markets have regained investors' faith which can be gauged from significant improvement in the market volume.

1.2 Research Problem

Corporate governance mechanism that is well practiced could benefit shareholder financially by exercising more control in the companies' management. Moreover, the corporate governance characteristic can be seen as proxies for independents and as the alignment of interest between management and the shareholder in minimizing the agency conflict.

Many researchers have examined among different countries to find out which factors could contribute to more disclosure by companies in their financial annual reports. Because disclosure of information helps to reduce cost of agency problems when there is an information asymmetry between management and shareholders. The present research therefore attempts to examine the relationship between corporate governance and disclosure via internet, specifically by investigating the impact of company size, profitability and leverage on the extent of IFR among UAE companies.

The efficiency gap has been narrowed in the world's major economies but there remain important gaps in what we know. In particular, we lack a sufficient understanding of the complicated ways in which the various corporate governance mechanisms interact with each other and with other characteristics of firms and economies. This type of research among Gulf countries is almost non-existing. Therefore, the research problem that is investigated in this study is especially focused on the current status of IFR in the context of UAE listed companies, and the factors that influence the extent of IFR among UAE companies.

1.3 Research Questions

1. Is there any significant relationship between company size and the extent of IFR among UAE companies?
2. Is there any significant relationship between the level of profitability and the extent of IFR among UAE companies?
3. Is there any significant relationship between leverage and the extent of IFR among UAE companies?

4. What is the current status of Internet financial reporting in the context of UAE listed companies?

1.4 Research Objectives

The main objective of this study is to examine which among the selected variables contribute to voluntary disclosure and which attributes drive management toward increase disclosure levels. Specifically, the objectives of this study are:

- To examine whether company size affects the extent of IFR among UAE companies.
- To examine whether level of profitability affect the extent of IFR among UAE companies.
- To examine whether leverage affects the extent of IFR among UAE companies
- To identify the current status of IFR among UAE companies.

1.5 Significance of Study

Since studies are almost non-existing among Gulf countries, it is worthy to examine the status of IFR among UAE companies. UAE government has been trying to improve its investment environment to make it more desirable for domestic and foreign capital funds. One of the improvements is on corporate financial disclosure. Increasingly, more and more companies disclosure their company's financial information through the internet. Without a doubt this form of dissemination facilitates and enables many parties like corporation, regulators, policy makers, the analytical and

empirical researchers and investors to be informed about up-to-date companies' publications or announcement of both financial and non financial information.

Lastly this research will improve the understanding on which corporate governance factors that affect the extant of voluntary disclosure. Information about this area via providing additional evidence on corporate governance and disclosure will definitely be disseminated more, faster, and more economical.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

Many studies have investigated the relationship between corporate governance mechanisms and firm's disclosure behaviors in view of the fact that separation of control and ownership is the major form of corporate governance. For instance studies with a wide range of research questions covering different countries and time periods have been carried out by Chow and Wong-Boren (1987), Hossain et al (1994), and Balach and Ran (2004).

Nowadays the beneficial parties seek the most efficient, cheapest and fastest tool of communications in order to get the information that they need. Therefore, companies are moving in the direction of using the internet for the distribution of financial or non-financial information which are available on the companies' website since the internet is a powerful communication device. This chapter highlights corporate governance, the agency theory, voluntary disclosure and its reasons, financial reporting evaluation in UAE, internet financial reporting, and the status of IFR among countries and the determinants of IFR.

2.1 The Agency Theory

Jensen and Meckling (1976) provide a framework in the agency theory connecting disclosure behavior to corporate governance. They define agency theory as a contract under which one or more persons (the principles) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent. Corporate governance mechanisms are created to control the agency problem between agents and principals which arise because of information asymmetry and ensure that managers act in the interests of shareholders.

Further, agency theory provides a framework for analyzing financial reporting incentive between managers and owners (Hossain, Perera and Rahman, 1995). In the agency theory one can observe that potential agency costs exists, where there is a separation of ownership and control of a corporation.

2.2 Voluntary Financial Disclosure

Financial disclosure consists of mandatory and voluntary disclosure (Penmann, 1988). Mandatory disclosure is defined as any financial items disclosed in companies annual reports that are prearranged by financial reporting standards and or stock exchange regulations. Meek, Reports and Gray (1995) define voluntary disclosure as disclosures in excess of requirements, which are not stated by the companies act to supply information that deemed related to the users decision needs of annual reports. The majority of studies were applied to developed countries to examine the relationship between level of disclosure and firms characteristics [examples are Buzby (1975) in the USA, Firth (1979) in the UK, and Cooke (1998) in Sweden, while in developing

countries such as in Egypt Ahmed and Nicholls (1994) and Mahmood (1999) in Bangladesh investigated the association between firm's characteristics such as industry type, firm size and the extent of disclosure.

According to Welker (1995), managers are not likely to withhold information for their own benefits under an intensive-monitoring environment, because this could lead to improvement in disclosure comprehensiveness and quality of financial statements. On the other hand, if the relationship is substitutive, companies will not provide more disclosures for more governance mechanisms since one corporate governance mechanism may substitute one another. If information asymmetry in a firm can be reduced because of the existing internal monitoring packages, the need for having additional governance devices is considered smaller. These apparently conflicting viewpoints on the impact of corporate governance have not been totally resolved, in spite of this theoretical ambiguity.

Companies that perform well have a strong incentive to report their operating results. Competitive pressures would also force companies to report even though they did not have good results. Silence of a failure to report would be reinterpreted as bad news. Companies with bad news would be motivated to report their results in order to avoid being suspected of having poor result. Such a situation would also force bad-news firms to disclose results in order to maintain credibility in the capital market.

2.3 Reasons and Incentives for Voluntary Disclosure

Management department of companies provides items in their quarterly or annual reports since they assume those items are important to be declared to meet the user's need of information. There are various groups of users of quarterly or annual reports with each group having different perception regarding voluntary items to make a decision making.

Accounting theory suggests that many reasons cause an organization to disclose items voluntarily to users. One such reason is centered on the need to raise capital at the lowest possible cost (Cooke, 1998). Good reporting is expected to lower firms cost of capital because there is less uncertainty in firms that reporting extensively and reliably. Therefore, there is less investments risk and lower required rate of return.

Healy and Palepu (2001) identify five pressures or hypotheses to managers' decisions to voluntarily disclosure information for capital market reasons. First, the capital market transactions hypothesis where firms have motivation to disclose voluntarily to reduce information asymmetry and ultimately reduce the cost of external financing by reducing information risk. Second, corporate control contest hypothesizes that when performance of an organization is running poorly, managers do provide voluntary disclosures in an attempt to increase firms voluntary and therefore reducing the risk of management job losses. Third, the stock compensation hypothesis states that managers who are rewarded with stock compensation have an incentive to use the voluntary disclosures in order to reduce the likelihood of insider trading allegations. Fourth, the litigation cost hypothesis, where the threat of litigation can encourage firms

to increase voluntary disclosure. In other words, managers have an incentive to disclose bad news to avoid legal actions for inadequate disclosure, this finding is consistent with that of Skinner (1994). The last pressure is the proprietary cost hypothesis which states that voluntary disclosure will be restricted if managers perceive that disclosure could be competitively harmful.

Voluntary disclosure for capital market reason also include the multiple listed companies which have an interest in foreign capital market since foreign operations are often financed by capital (Choi and Mueller. 1992). In addition, companies may have attained their status on the securities market and are able to attract new shareholders for raising funds because they act responsibly (Cooke, 1998).

2.4 Internet Financial Reporting

Ashbaug et al. (1999) define Internet Financial Reporting (IFR) firms as those that provide in their websites either: (1) a comprehensive set of financial statements (including footnotes and the auditors' report); (2) a link to their annual reports elsewhere on the Internet or (3) a link to the US Security and Exchange Commission's (SEC) Electronic Data Gathering, Analysis and Retrieval (EDGAR) system.

Extensive use of the internet as a medium of Web-based business reporting for disclosure purposes encouraged major regulators in developed regions like USA and Canada to establish the electronic filing systems. In 1993, the US Security and Exchange Commission (SEC) adopted the Electronic Data Gathering, Analysis, and Retrieval system (EDGAR) (Wallman, 1997). EDGAR system performs automated

collection, validation, indexing, acceptance, and forwarding of submissions by companies and others who are required by law to file forms with the SEC (http://www.sec.gov/index). In 1997, the Canadian Securities Administrators developed the System for Electronic Document Analysis and Retrieval (SEDAR) which is an electronic filing system meant for the disclosure documents of public companies and mutual funds across Canada (http://www.sedar.com).

Extensible Business Reporting Language (XBRL) is the recent introduction main footstep in the Web-based business reporting field. XBRL is being developed by an international non-profit consortium of approximately 250 major companies, organizations and government agencies.

XBRL is an electronic communication of business and financial data set to revolutionize business reporting around the world. It provides many benefits; first in the analysis, preparation and communication of business information, second, it offers reliability and improved accuracy and greater efficiency to all those involved in supplying or using financial data (www.xbrl.org), third, it enhances the ability of users to exchange financial information between different software applications electronically, and fourth, XBRL speeds up the ability of users to compare financial information, including accounting policies, notes to the financial statements and other text items.

2.5 The Status of IFR among Countries

A number of studies have investigated the use of Internet as an instrument for the disclosure of financial information with a wide range of research questions covering different countries and time periods. Among the earliest studies was one conducted by Louwers, Pasewark and Typpo (1996) who noted that the future of online financial reporting might involve extending disclosure beyond the reproduction of a print-based annual report, improving timeliness, and permitting a high degree of interactive retrieval of information.

Lymer et al (1997) finds that the top 50 companies on the London Stock Exchange that 92% (46 companies) had a Web server and 52% disseminated accounts or reports on their home page. Furthermore, the study shows that companies in the banks, financial services and insurance sectors provide limited financial information compared with the chemicals and pharmaceuticals sector. Gray and Debreceny (1997) studied the use of the Internet among US companies listed in the Fortune 50. They find that 98% of US companies had a Web site, 68% had Web-based annual reports, and 36% disclosed auditor reports on the Web.

Lymer and Tallberg (1997) examine the usage of the Web for corporate reporting by companies based in UK and Finland. They also addressed the issue of whether there were significant differences between the levels and types of usage by companies in these two countries. They find that 90% of the 72 companies listed on the Helsinki Stock Exchange had Web sites. However, their potential for disseminating

financial statements remained vastly underdeveloped, especially in Finland where the use of the Web for reporting was rather limited compared to the UK.

Companies consider the Internet as an important medium to disseminate financial information. Petravick and Gillet (1998) chose a sample of 125 Fortune 500 companies to examine how quickly companies posted earnings releases on their Web sites. They report that 79.2% (99 of 125) of these companies made the releases available through their Web sites on the same day as the announcement.

Trites (1999) surveyed 370 companies randomly chosen from 10,000 companies listed at the New York Stock Exchange, the NASDAQ and the Toronto Stock Exchange. They find that 69% of these companies had a home page and 35% of them included some form of financial information on their Web site.

Deller, Stubenrath and Weber (1999) investigated the top 100 companies in the US, UK and Germany. The study indicates that the US companies offer better investor relations information via the Internet than their counterparts in the UK and Germany.

A study in Spain by Gowthorpe and Amat (1999) showed the status of Web reporting by the 379 companies listed at the Madrid Stock Exchange. 16% (61 companies) had an accessible Web site, and of these 61 companies, only 34 (55.7%) provided some form of financial information on their home page.

Marston (2003) find that 78 (79%) of 99 Japanese companies had a Web site in English. 68 (87%) companies of these 78 companies reported some financial information with 57 (73%) providing detailed accounting information.

The state of Web reporting in Malaysia is described in a study by Ismail and Tayib (2000) of 237 Malaysian listed companies. They find that 218 companies (92%) had Web sites. Of the 218 companies, only 25 (11.5%) of the companies disclose their full annual reports.

A comparative study was conducted by Joshi and Jawaher (2003) on a total of 75 companies (Kuwait 42 and Bahrain 33), firstly to investigate the extent of Internet financial disclosure of Kuwait listed companies and Bahrain listed companies and, secondly to examine the variables that strongly affect the decisions for including such information. They find that 47.6% of Kuwait companies had websites compared to 48.5% of Bahrain companies.

A recent Malaysian study by Abdul Hamid (2005) with a sample comprising 100 stock market index-linked firms listed on the Kuala Lumpur stock exchange. The results indicate that 95 % of these companies provided investor relation information via Internet.

Future IFR may include the use of multimedia, such as sound, animation and video to potentially increase the understanding of information.

2.6 Determinants of IFR

One of the earliest empirical studies that examine firms' adoption to different Internet financial reporting strategies was conducted in the USA by Ashbaugh, Johnstone, and Warfield (1999). 290 American companies were obtained from the Association for Investment Management and Research (AIMR) in its 1994/1995 and 1995/1996 annual reports. Four independent variables were selected with regard to the firm's specific characteristics: firm's size, return on assets, AIMR rating and percentage of shares held by individual shareholders (total shares outstanding). They find that IFR has become a common practice for most firms and IFR firms are larger in size, have good operating performance and are normally rated as excellent firms by AIMR compared to non-IFR firms.

A similar study in Portugal by Rodrigues and Carlos (2001) investigates whether Portuguese firms follow the universal trend of IFR of other countries, and attempt to associate IFR practices with firms' specific characteristics. A sample consisting of 74 firms was chosen randomly from the firms listed in the Lisbon and Porto stock Exchange. IFR firms were denoted as firms having financial disclosures, summarized financial statements, chairman statements, reports and accounts and management reports in their Web site. Statistical analyses used in this research were descriptive and chi-square tests. Three independent variables were selected with regard to the firm's specific characteristics: firm size, industry type and overseas listing by Portuguese incorporated firms. Overseas listing results were excluded as they violate the assumption of chi-square test due to the small number of Portuguese firms that were listed in the overseas market. The analysis on the industry type is found to have no

significant influence on IFR practices. Firm size is the only significant factor that is associated to IFR firms. The authors also find that IFR is growing progressively by Portuguese firms.

Ettredge, Richardson, and Scholz (2002) examined 220 US companies to see whether there was a relationship between the extent of Web site disclosure and firm-specific determinants. They find that 193 companies had a Web site disclosure level and were positively related to firm size, raising equity capital and negatively related to the correlation between earnings and returns.

The findings of a survey by Debreceny, Gray, and Rhaman (2002) on 660 companies in 22 countries show that firm-specific characteristics such as firm size, listing on US stock exchanges by non-US firms, firm's level of technology and growth prospects are significantly related to the practice of IFR. Other firm characteristics such as market risk, leverage and listing of the firm on overseas securities markets were not significantly associated with IFR practices.

Oyelere, Laswad and Fisher (2003) conducted a study in New Zealand on 229 New Zealand companies using A multivariate linear regression analysis Seven independent variables (firm size, liquidity, industrial type, spread of shareholding, leverage, profitability and internationalization) were selected with regard to firm's characteristics.). Their findings show that size, liquidity, industry sector and spread of shareholding are the primary determinants of IFR practices among New Zealand

companies. However, other firm characteristics such as leverage, profitability and internationalization associated with voluntary reporting, are not related to IFR.

In a sharp contrast, Marston (2003) studied the factors that affect IFR practices among Japanese companies. Four independent variables were selected namely firm size Profitability, Industry type, overseas, and listing status. The results indicated that there is no relationship between such factors and IFR in Japan.

Joshi and Jawaher (2003) examined whether there was a relationship between the extent of Web site disclosure and firm-specific determinants among Bahrain and Kuwait listed companies. Six independent variables were selected with regard to firm's characteristics: company size, profitability, debt ratio, industry type, auditor size, and country effect. They find that the major factors influencing financial reporting on the Internet are firm size and industry type. However, other firm characteristics associated with voluntary reporting, such as profitability, debt ratio, auditor size and country effects do not affect IFR.

A recent study on 3 Latin countries (Argentina, Brazil and Mexico) by Abdul Hamid (2005) applied multivariate analysis to find out the association between the firm value and voluntary disclosure of financial information. Results on the sample of 150 companies show that there is a significant positive association between disclosure of financial information on the Internet and market value, with the association directly influenced by industry sector and size of the company regardless of the country in which it operates.

The above discussion from previous studies reveals that there are four dominant variables with respect to the extent of IFR. These factors are size of company, profitability, leverage, and industry type. The results show a positive significant relationship between firm size and the extent of IFR but no significant relationship with profitability and leverage. In terms of industry type, results are mixed on the extent of IFR.

CHAPTER THREE

METHODOLOGY

3.0 Introduction

Upon existing academic literature several determinants explain why a firm may provide more information voluntarily than mandatorily.

This chapter covers the theoretical framework, hypotheses, model specification and measurements of variables, disclosure index development and finally presentation of the model.

3.1 Variables and Framework

3.1.1 Disclosure Index (IFR)

There is no agreed theory on the number and selection of items that should be included in a disclosure index. Cooke and Wallace (1989) argue that the measurement of accounting disclosure is a procedure that has some inherent limitations and subjectivity. To reduce the subjectivity, the literature suggests that the following steps should be taken into consideration when constructing the index (see for example Hossain et al 1994).

Disclosure level can be measured in a number of different ways. The commonly used approach has been adopted using a discretionary item scores “1” if it is disclosed, and “0” if it is not disclosed. This method of scoring is known as the unweighted

approach based on the assumption that each item of disclosure is equally important. An unweighted approach has been used in several prior studies (see for example, Wallace, 1988, and Cooke, 1998) in their studies when employing unweighted disclosure index. Gul and Leung (2004) report that the final disclosure list contained 44 discretionary items. Some of these are background information, financial performance information and non-financial performance information. The background information includes matters that cover corporate goals, competition, products and markets. On the other hand, performance information includes items such as changes in sales, gross profits and R&D expenditures. Non-financial information also includes number of employees, and staff training and products segment analysis. For each item in the disclosure index, the company receives a score of ‘‘1’’ if it voluntarily discloses information on the item and ‘‘0’’ if otherwise.

Balach and ran (2004) measures the disclosure score index that comprises the consideration of 66 discretionary items. The study used approximately 60% of the discretionary items as applied in previous studies. Further, Ho and Wong (2001), measure also the reported disclosure by using a relative disclosure index. It is derived by first compiling a comprehensive list of voluntary disclosure items that companies may provide in their annual reports in Hong Kong. The index consists of a total of the most important 20 items that are disclosed in annual reports.

In the present study, the extent of voluntary disclosure is measured by using a disclosure index which contains items that are disclosed in the annual report. In this

study the voluntary disclosure is represented by internet financial reporting. The total scores of the extent of IFR would range from "0" (if they do not publish any one of the eight types of information) to "8" (if they publish all). These 8 items are selected because they are commonly used in the previous studies.

3.1.2 Firm Size

It is assumed that large firms are more likely to disclose more information than small firms. Due to the complexity structures of large firms, more information is needed to the users for good decision makings. Agency theory suggests that larger firms have higher agency costs compared to the smaller firms (Watts and Zimmermann, 1978).

Voluntary disclosure can reduce the agency costs. Buzby (1975) suggests that collecting and disseminating information are costly exercise; smaller firms do not have sufficient resources for collecting data and incentives for web-based disseminating hence only larger firms could afford such expense. Moreover Watts and Zimmermann (1978) argue that larger firms face higher politician costs and voluntary disclosures are a possible tool to reduce these costs. Firth (1978) examines the impact of firm size, stock market listing, and auditor's presence on voluntary corporate disclosure and finds that firm's size and stock market listing are positively associated with voluntary disclosure. McNally et al (1982) find that company size has significant relationship with the level of voluntary disclosure items. Hossain et al (1994) find that firm size and ownership structure of foreign-listing status are statistically related to the level of

information voluntarily disclosed by publicly traded companies. Therefore it is hypothesized that:

H1: There is a relationship between firm size and the extent of IFR

3.1.3 Profitability

Foster (1986) suggests that profitable firms have incentives to distinguish themselves from less profitable firms in order to raise capital on the best available terms by providing voluntary disclosure. The companies seek to achieve this by post voluntary disclosure on their web sites. In addition managers are motivated to disclose more detailed information to support their position and remunerations. Haniffa and Cook (2002) find a positive and significant association between firms' profitability and the extent of voluntary disclosure. Lev and Penman (1990) argue that investors perceived non-disclosure of information as bad news, therefore good-news firms have the motivations to be out from other bad firms. This means that when there is increase in profitability, the voluntary disclosure of these firms will increase. This provides the basis for the second hypothesis:

H2: There is a relationship between profitability and the extent of IFR.

3.1.4 Leverage

Leverage is the degree to which an investors or businesses utilize borrowed money. For investors, leverage means buying on margin or using derivatives such as option to enhance return on value. But for companies, leverage is measured by

dividing total debt by total assets. The more total debt, the grater the financial leverage and the greater the risk of the company falling on its face.

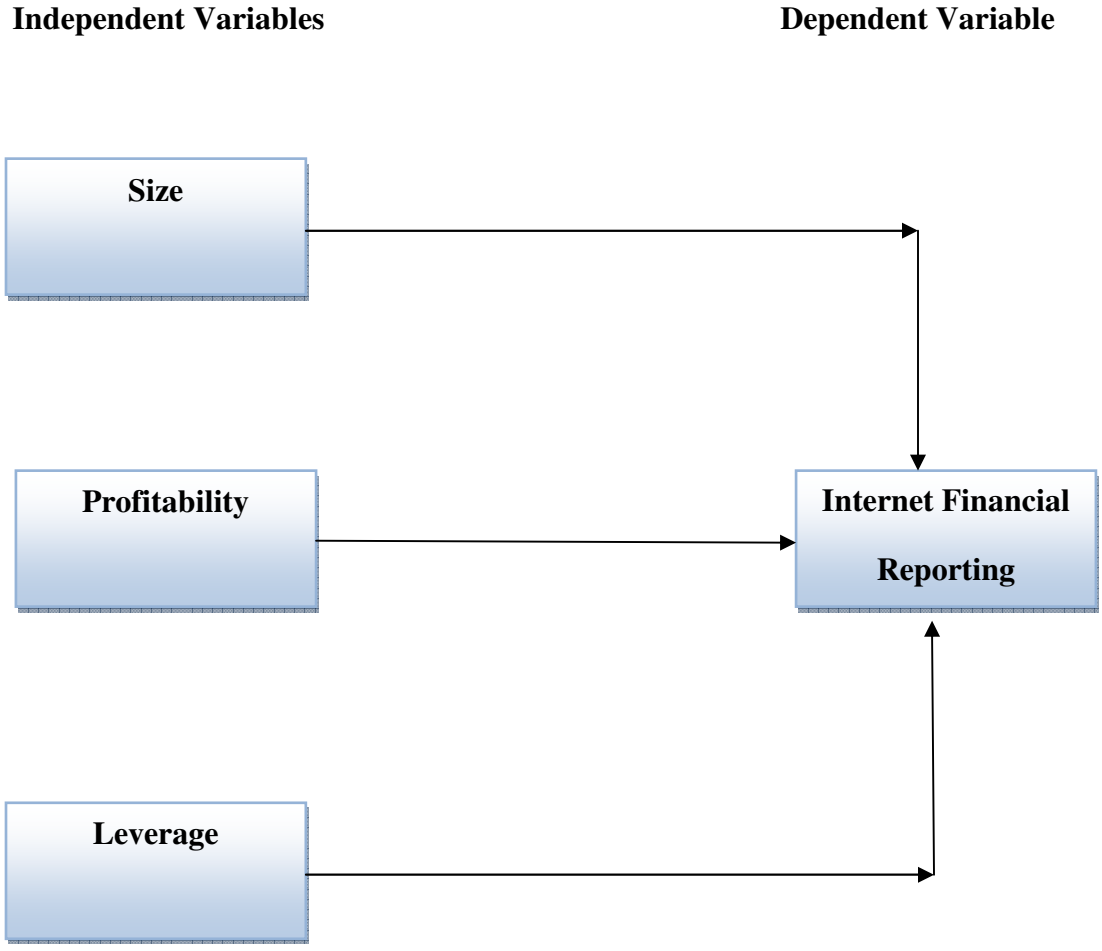
Leveraged investing can be extremely risky because investors can lose not only their money but the money they borrowed as well. Voluntary disclosure of information concerning debt fund may allow shareholders and bondholders to make better predictions about the growth, risk and return prospects of companies. Therefore, firms with higher leverage tend to disclose more information than the lower ones. Cadbury (1995) finds that there is a positive association between leverage and the extent of voluntary segment disclosure among New Zealand firms. Jensen and Meckling (1976) argue that the more highly leveraged firms incur higher monitoring cost. Management therefore might choose voluntary IFR for monitoring purpose, It is thus hypothesized that:

H3: There is a relationship between leverage and the extent of IFR.

3.2 Framework

Considering all factors of the independent and dependent variables, the model of the study is depicted in the following figure.

Figure 3.1: Theoretical Framework



3.3 Measurement of Variables

3.3.1 Dependent Variable

This study has one dependent variable i.e. the extent of internet financial reporting (IFR). This variable is defined as the number of financial information published on the Internet. For the purpose of this study, eight types of financial information are identified to measure the extent of IFR. This information is financial highlight, audit report, balance sheet, income statement, statement of shareholder equity, cash flow, accounting notes, and interim report. The total scores of the extent of IFR would range from "0" (if they do not publish any one of the eight types of information) to "8" (if they publish all**).** These 8 items are selected because they are commonly used in previous studies.

3.3 .2 Independent Variables

3.3.2.1 Firm Size

Size is the most dominant factor that has been identified to influence the extent of IFR (Ettredge et al, 2002; Martson, 2003; and Wesley and Luiz, 2004). Size of a company can be measured in a number of ways, such as capital employed, turnover, number of employees, and company's market value. There is no overriding theoretical reason for selecting one rather than another. For example, Firth (1979) used sales turnover and capital employed to measure the company size, and Cooke (1991) applied number of shareholders, total assets and turnover to measure the size of the company. Following Ashbaugh et al. (1999), this study uses total assets to measure the size of the company.

3.3.2.2 Profitability

In order to test the relationship between profitability as independent variable to the number of financial disclosure via Internet as dependent variable, this study follows Xiao et al (2004) who measure profitability variable using return on assets (ROA). This is done by dividing the net profit or loss by total assets.

3.3.2.3 Leverage

Following Xiao et al. (2004), this study measures firm leverage by dividing the total of liabilities by total assets. The long-term liabilities plus the current liabilities equal to total of liabilities.

Table 3.2: Definition and Measurement of Variables

Dependent Variable	**Definition**	**Measurement**
IFR(Internet financial reporting)	The extent of IFR	Total number of points awarded for voluntary discloser, strategic, non-financial and financial information (with score ranges from "0" (no financial disclosure) to "8" (full financial disclosure).
Independent variables	**Definition**	**Measurement**

ROA	Profitability	Return on Assets
Size	Firm size	This variable is measured by the log (base ten) of total assets
LEV	Leverage	The ratio of total debt of total equity value of the firm

3.5 Data Collection

Secondary data was collected, obtained from the information disclosed in the given firms' web sites. The main advantage of using the internet is because information obtained is cheap and quicker to collect compared to obtaining primary data (Zikmund, 2003). The main purpose of the current study is to examine the state of financial reporting through internet among UAE companies, as well as determining the factors that influence the companies to use such means for financial disclosure. This is done by first identifying companies' web sites and then examining the contents (i.e. financial information) of each web site. In order to do this, many search engines were used such as Google and Yahoo.

3.5.1 Sample Selection

The population of this study consists of all the 125 firms that are listed in UAE stock market in 2007. These firms are classified into four sectors: industrial (25 companies) services (33 companies), banking (19 companies) and insurance (23 companies). The final sample consists of 88 firms with websites because 25 firms disclosed their financial reporting in foreign currency (i.e. not in Emirates dirham), and

12 firms did not have websites. Therefore 37 firms are excluded from the 125 public listed companies in UAE in 2007. The year 2007 is chosen as the base year because that year's annual reports formed the latest source of information available at the time this study was initially conducted.

3.6 Data Analysis

3.6.1 Descriptive Analysis

This descriptive study produced the mean, minimum, maximum and standard deviation for each variable for UAE companies.

3.6.2 The Correlation of Variables

This study shows how one variable is related to another. The results of this analysis represent the nature, direction and significant of the correlation of the variables used in this study and the correlation between variables is analyzed by using the person correlation.

3.6.3 Model Specification and Multiple Regression

The multiple regression method is used to examine the relationship between the extent of IFR in UAE companies and firm size, profitability and leverage. The result of regression analysis is an equation that represents the best prediction of a dependent variable from several independent variables.

This method is used when independent variables are correlated with one another and with the dependent variable.

The following regression equation is estimated as follow:

$$\mathbf{X = \alpha + \beta 1size + \beta 2Lev + \beta 3Prof}$$

Where:

X	=	dummy variables, the score ranges from"0" (no financial disclosure) to "1" (full financial disclosure)
α	=	constant
Size	=	measured by total assets.
Profitability	=	measured by net profit or loss divided by total assets.
Leverage	=	measured by total liabilities divided by total assets.

In this model, all independent variables enter the regression equation at once to examine the relation between the whole set of predictors and the dependent variable. The aim of this analysis is to determine which independent variables are highly significant to determine the company's profitability.

CHAPTER FOUR

ANALYSIS AND FINDINGS

4.0 INTRODUCTION

This chapter highlights the results of the study. The results comprise descriptive statistics, correlations and regression employed to determine the relations among the variables (independent and dependant).The results are made possible through the usage of SPSS software version 11.5 and Microsoft Excel.

4.1 ANALYSIS

4.1.1 Descriptive Statistics

There were 125 publicly listed companies on UAE stock market as of 2007.

25 firms are excluded because they disclosed their financial reporting in foreign currency (i.e. not in Emirates dirham), Another 12 firms are further excluded because they did not have websites. The final sample consists of 88 firms with web sites. Table 4.1 shows all the four type of industries based on UAE's stock market classification. The results in Table 4.1 show that the two largest sectors are services (33%) and industrial (25%).

The findings with respect to the existence of the companies' web sites and the disclosure of the financial information in those Web sites are presented in Tables 4.2 and Table 4.3. The results show that 88 out of 100 (88%) of UAE public listed companies have Web sites.

Table 4.1: Type of Industry Classification-

UEA Stock Market (2007)*

Sector	Number of Firms	Percentage
Services	33	33%
Industrial and hotels	25	25%
Insurance	23	23%
Banking	19	19%
Total	100	100%

*25 firms were excluded because of their financial reporting were in foreign currency

Table 4.2: Internet Usage by UAE Listed Companies

Items	Number of Firms	Percentage
Web site	88	88%
No Web site	12	12%
Total	100	100%

Table 4.3: Financial Information Provided via 88 Internet Web Sites

Item	Number	Percentage
Financial Highlight	6	6.82%
Auditor Report	87	98.86%
Balance Sheet	88	100%
Income Statement	88	100%
Statement of Stakeholder Equity	86	97.73%
Cash Flow Statement	88	100%
Accounting Notes	87	98.86%
Interim Report	67	76.14%

In Table 4.3 above, it is observed that all 88 firms declared balance sheet, income statement, and statement of stakeholder equity on their websites. It also can be seen that the lowest internet reporting is on financial highlight (only 6.82% i.e. 6 out of 88 websites).

Table 4.4: Financial Information Provided via Internet
(% in brackets)

Items	Financial Highlight (FH)	Auditor Report (AR)	Balance Sheet (BS)	Income Statement (IS)	Statement of Stakeholder Equity (SSE)	Cash Flow Statement (CFS)	Accounting Notes (AN)	Interim Report (IR)
Services	2(0.33%)	27(0.31%)	28(32%)	28(32%)	27(31%)	28(32%)	27(31%)	18(27%)
Industrial and hotels	1(0.17%)	23(26%)	23(26%)	23(26%)	22(26%)	23(26%)	23(26%)	17(25%)
Insurance	2(0.33%)	19(22%)	19(22%)	19(22%)	19(22%)	19(22%)	19(22%)	16(24%)
Banking	1(0.33%)	18(21%)	18(20%)	18(20%)	18(21%)	18(20%)	18(21%)	16(24%)
Total	6	87	88	88	86	88	87	67

Table 4.5: Financial Information Published via Internet by Industry type

Sector	FH	AR	BS	IS	SSE	CFS	AN	IR
Services	2	27	28	28	27	28	27	18
Industry	1	23	23	23	22	23	23	17
Insurance	2	19	19	19	19	19	19	16
Banks	1	18	18	18	18	18	18	16
Total	6	87	88	88	86	88	87	67

Tables 4.4 and 4.5 refer to the type of financial information presented on the companies' web sites. The most commonly found financial information is the balance sheet, income statement and cash flow statement, all of which were disclosed by the 88 companies (100%). Accountant's notes and Auditor reports were disclosed by 87 companies (98.8%). Interim report was disclosed by 67 companies (76%), in addition to statement of stakeholders equity which was disclosed by 86 companies (97.7%). The

lowest declared items were financial highlights which were disclosed by 6 companies (6.8%).

Descriptive analysis is to describe the response for the major variables under the study such as, mean and standard deviation on the dependant variable and independent variables obtained. The results of the descriptive analysis are shown in the following Tables 4.6, in addition to the results of the descriptive analysis for the whole sample of the companies listed in UAE's stock exchange.

Table 4.6: Descriptive Analysis for Dependant Variable and Independent Variables (All companies)

	N	Range	Minimum	Maximum	Mean	Std. Deviation
IFR	88	1.0000	.0000	1.0000	.068182	.2535021
ROA	88	1.29411	-.20360	1.09051	.1010751	.13466040
LEV	88	12.89541	-1.17590	11.71951	1.8715953	2.67580723
SIZE	88	9.518590	16.142243	25.660834	21.688709 66	1.962550513
Valid N (listwise)	88					

From the results in Table 4.1, it can be observed that the means for the all variables are between a minimum of 0.000 (IFR) and maximum 25.66 (size of the companies). However, it can be observed also that the standard deviations are between a minimum of 0.134 (ROA) and a maximum of 2.67580723 (leverage of the companies).

4.1.2 Correlation

Correlation analysis is executed to test the strength of relationships between variables. Statistical test at 5% level is used to test the significance of the relationships between the independent variables in this study. It is also used to examine the potential issue of multicollinearity that exists when two explanatory variables are highly correlated. Table 4.7 shows the correlation matrix among the independent variables.

Table 4.7 Correlation Matrix among Independent Variables

		IFR	ROA	LEV	SIZE
IFR	Pearson Correlation	1	-.096	-.014	.280(**)
	Sig. (2-tailed)	.	.374	.895	.008
	N	88	88	88	88
ROA	Pearson Correlation	-.096	1	-.311(**)	-.230(*)
	Sig. (2-tailed)	.374	.	.003	.031
	N	88	88	88	88
LEV	Pearson Correlation	-.014	-.311(**)	1	.549(**)
	Sig. (2-tailed)	.895	.003	.	.000
	N	88	88	88	88
SIZE	Pearson Correlation	.280(**)	-.230(*)	.549(**)	1
	Sig. (2-tailed)	.008	.031	.000	.
	N	88	88	88	88

** Correlation is significant at the 0.01 level (2-tailed).
* Correlation is significant at the 0.05 level (2-tailed).

. It can be seen from Table 4.7 that except for size with leverage which is slightly more correlated at 0.549 and significantly positive, the other correlations between the independent variables were quite low. . The correlation matrix is a powerful tool for getting a rough idea of the relationship between predictors (Alsaeed, 2005). If Pearson correlation result is higher than 0.7, then there is relation among independent variables (Anderson, Sweeney, and Williams, 1996). Since all the Pearson

correlations between the independent variables are lower than 0.7, therefore there is no multicollinearity problem.

4.1.3 Regression analysis

Regression analysis for all observation

Table 4.8: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F Change	df1	df2	Sig. F Change
1	.354(a)	.126	.094	.2412569	.126	4.019	3	84	.010

a Predictors: (Constant), SIZE, ROA, LEV

R square is the relative predictive power of a model and it is a measure between 0 and 1. In this analysis, it can be seen that the R square is 0.126 indicating that 12.6 percent variation in the IFR is explained by the three independent variables (size, profitability, and leverage).

Table 4.12 shows the regression analysis for all observation. It can be observed that size of the companies is a significant variable. Multicollinearity is not a problem since the VIFs are less than 10.[1]

[1] Multicollinearity exists when one or more of the explanatory variables are highly collinear with other variables in the regression model. In this study, each of the explanatory variables is regressed on the remaining explanatory variables to compute R square values

Table 4.9 Regression Analysis for All Observations
Coefficients (a)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95% Confidence Interval for B		Collinearity Statistics	
		B	Std. Error	Beta			Lower Bound	Upper Bound	Tolerance	VIF
1	(Constant)	-1.005	.336		-2.994	.004	-1.672	-.337		
	ROA	-.159	.203	-.084	-.784	.435	-.562	.244	.898	1.113
	LEV	-.025	.012	-.263	-2.099	.039	-.049	-.001	.663	1.509
	SIZE	.052	.016	.405	3.311	.001	.021	.084	.695	1.439

a Dependent Variable: IFR

4.2 Summary of the Chapter

The output indicates that only size (as measured by total assets) contributed significantly to internet financial reporting, therefore hypothesis 1 is accepted. However, profitability and leverage are insignificantly correlated with the extent of IFR and thus hypothesis 2 and hypothesis 3 are rejected.

Based on the results it can be concluded that statistically there appears to be a significant positive relationship between size of companies and the extent of IFR. However, it is also evident that there is no significant relationship between either profitability or leverage and the extent of IFR.

CHAPTER FIVE

CONCLUSION

5.0 CONCLUSION

Internet is increasingly providing companies and extending s the scope with enormous prospects and opportunities through which they can voluntarily deal with information streaming to various groups of external users. Through companies' corporate servers, internet can provide vast quantities of information, both financial and non-financial, which users require for easily access.

The main purpose of this study is to provide insights into the use of internet for disseminating financial information among UAE listed companies and to put some lights on the factors that affect such companies in adopting financial disclosure through internet.

Regarding the primary objective of this study, and despite the fact that 88 of UAE listed companies have websites; the findings show that UAE companies are still to some extent placed behind those in other developed countries such as the US, UK and Japan companies and even with other developing countries like Malaysia. Thus, related institutes such as UAE Accounting Association (SAA) should play a more active role in promoting UAE companies initiatives to voluntarily disclose their financial information on the internet. This is important as the extent of IFR could boost

the confidence of investors both locally and globally to invest in UAE business companies.

With respect to the factors that affect companies adopting internet-based financial reporting, this study examined three factors namely firm size, leverage and profitability. A linear regression analysis is applied for this purpose. Findings reveal that profitability and leverage do not significantly influenced internet financial reporting. These findings are similar to those found by Debrecency et al. (2002) and Joshi and Jawaher (2003).

The result also shows that there is a significant positive linkage between the amount of financial disclosure through internet and size of companies. This finding is consistent with prior studies such as Ashaugh et al. (1999), Debrecency et al. (2002), Marston, (2003), Joshi and Jawaher, (2003) and Wesley and Luiz, (2004). Prior studies have argued that larger firms are more inclined to adopt voluntary disclosure practices including the IFR due to the proposition of agency theory (e.g. higher cost due to larger number of shareholders), the need more capital, and ability to sustain incremental cost for disclosure due to the huge resources held and political cost theory (e.g. higher regulation by the regulatory authorities).

While this study attempts at providing an insight into the status and determinants of IFR among UAE companies, it is also subject to several limitations. Due to the limited time in which this study is carried out, only three factors (size, profitability and leverage) that might explain the reporting practices of companies on

the internet are examined. . Further research should also include other possible factors such as level of IT, auditor size and firm value that could further explain the extent of IFR among UAE companies.

5.1 Recommendation

Future research might extend the scope of this study by involving comparative studies with other Arabic countries. Nevertheless, hopefully, the results of this study will provide some insights into the online disclosure practices of UAE companies and will be a starting point for further research in this area.

Finally, the future of financial reporting on the Internet will not be just about providing traditional information, it is expected that future Internet disclosures are more likely to provide certain advantages over the traditional annual reporting by improving timeliness, expanding the scope of company corporate information to the public, allowing a degree of interactivity, and also projected to find annual financial data on an updated monthly basis or on a rolling basis. Many companies are already providing 'investor relations' services in addition to basic financial statements. Users can sign up for copies of all company announcements and press releases to be e-mailed to them after they hit the stock exchange screen.

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