

THE UNIVERSITY OF HULL

THE EVOLUTION OF ACCOUNTING IN SAUDI ARABIA: A STUDY OF
ITS RELEVANCE TO THE SOCIAL AND ECONOMIC ENVIRONMENT

being a Thesis submitted for the Degree of
Doctor of Philosophy
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by

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بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ

In the Name of Allah,
Most Gracious, Most Merciful.

DEDICATION

To my mother, Rayegh

Whose affection, patience, encouragement, and prayers were continually with me throughout the stages of my education both at home and abroad.

I ask Allah to reward her with paradise in the day after.

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ABSTRACT

The need to study the evolution of accounting in its environmental setting in developing countries is increasingly recognised in the literature. The purpose of this thesis is to examine the evolution and status of accounting systems in developing countries, with particular reference to the Saudi Arabian environment. It attempts to highlight the main shortcomings in each component of the accounting system (education, profession, enterprise, government and national accounting) and to put forward suggestions and recommendations for improvement which reflect the socio-economic development needs.

The study has shown that Saudi Arabia is a developing country which has adopted a comprehensive development planning approach as its vehicle towards growth and socio-economic development, and its accounting system should serve this objective. In effect, however, the prevailing accounting system and practice in Saudi Arabia, including the recent developments, are based on the Anglo-Saxon accounting system, which is described as being complex to operate, particularly in a country with a relatively less sophisticated accountants' audience; its emphasis upon the external reporting and external auditing; and its virtual exclusion of government or public sector needs.

In contrast, the study suggests that most accounting shortcomings in Saudi Arabia would be alleviated by the adoption of a uniform accounting system, as such a system would facilitate the collection, storage and communication of accounting data, and facilitate the training process and transfer of "know-how" and skills. It was also found that the prevailing conditions and circumstances of the accounting environment in Saudi Arabia indicate that a national uniform accounting system would be both desirable and feasible. These conditions and circumstances include, among other things, centralised development plans, the need for economic development, the small size of the private sector, the relatively low accounting education level, the weakness of the accounting profession, and the low level of management training.

However, because such a system is likely to take a long time to establish, a plan for improving the current accounting system is proposed. The plan is based upon the socio-economic development needs of Saudi Arabia, which urgently require simultaneous improvements of all components of the accounting system noted above, by integrating them into a single framework of action. The plan assumes the willingness of accounting academicians, public accountants, and government officials, particularly those involved in planning, implementation, and control of the economic and financial activities of

the country, to participate in the accounting improvement process. Moreover, the proposed plan should be viewed as a part of the overall five-year economic development plan which already exists.

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LIST OF ABBREVIATIONS

AAA	American Accounting Association
AICPA	American Institute of Certified Public Accountants
APB	Accounting Principles Board
ASCA	Arab Society of Certified Accountants
CAA	Central Accounting Agency (Egypt)
CDS	Central Department of Statistics
EDA	Economic Development Accounting
EEvA	Economic Evaluation Accounting
FASB	Financial Accounting Standard Board
FRA	Financial Representative Administrative
GAB	General Audit Bureau
GBD	General Budget Department
GCC	Gulf Cooperation Council
GDP	Gross Domestic Product
GOTEVT	General Organization for Technical Education and Vocational Training
GPGE	General Presidency for Girls Education
HCAR	Higher Committee for Administrative Reform
IASC	International Accounting Standards Committee
IMF	International Monetary Fund
IPA	Institute of Public Administration
LDCs	Less Developed Countries
KACST	King Abdul Aziz City for Science and Technology
KAU	King Abdul Aziz University
KSA	King Saud University
KFUPM	King Fahd University of Petroleum and Minerals
MEED	Middle East Economic Digest
MOEI	Ministry of Industry and Electricity
MOAW	Ministry of Agriculture and Water
MOC	Ministry of Commerce
MOE	Ministry of Education
MOFNE	Ministry of Finance and National Economy
MOHE	Ministry of Higher Education
MOP	Ministry of Planning
OPEC	Organisation of Petroleum Exporting Countries
PIF	Public Investment Fund
PPBS	Planning Programing Budgeting System
PWI	Price Waterhouse International
R&D	Research and Development
REDF	Real Estate Development
SAA	Saudi Accounting Association
SAAB	Saudi Arabian Agricultural Bank
SABIC	Saudi Arabian Basic Industries Corporation
SAMA	Saudi Arabian Monetary Agency
SCIs	Specialized Credit Institutions
SIDF	Saudi Industrial Development Fund
SR	Saudi Riyal (\$ = 3.75 SR)
TAT	Transfer of Accounting Technology
TES	Two-Tiered Education System
UK	United Kingdom
UN	United Nations
USA	United States of America
ZITD	Zakat and Income Tax Department

PART I

BACKGROUND TO THE STUDY

CHAPTER 1

INTRODUCTION AND OUTLINE OF THE STUDY

1.1 Background to the Problem

It is argued that any changes in the accounting environment should be met with changes in accounting to keep pace with that environment. Since 1970, the accounting environment in Saudi Arabia, based on consecutive five-year development plans, has been changing rapidly. These changes have affected almost all aspects of Saudi life, particularly education, health, infrastructure and national product diversification (Elkharouf, 1985).

Unfortunately, accounting has not kept pace with the complexity, diversity, and progress of the Saudi socio-economic environment. This was confirmed recently by members of the team appointed to develop accounting in Saudi Arabia. In their Analytical Study (1986, para 3), they stated:

"We find that profit-oriented enterprises have changed considerably in size and their relationship with employees has reached an unprecedented level of complexity in the Kingdom. The accounting and auditing profession has not kept pace with complicated changes in the business sector."

In addition, accounting development has not been specifically incorporated into any of the development plans implemented so far except for the introduction of a few regulations, which merely prescribe the requirements and procedures for licensing accountants to practise and

outline the rules to be followed after licensing (see chapter 5).

Indeed, it is only in recent years that the Ministry of Commerce has recognized the serious deficiencies in the accounting field and the detrimental consequences, not only for individuals, but also for the national economy as a whole. As a result, the Ministry immediately agreed to finance a project to develop accounting in Saudi Arabia. The output of the first phase of the project has already been published in two volumes, the first entitled "Accounting Objectives and Concepts", and the second, "Auditing Standards".¹

However, analysis of these two volumes revealed that they include some accounting and auditing guidelines similar to those of the UK and USA, with emphasis placed upon the information needs of external users (mainly private shareholders), while little or no consideration has been given to the information needed by the government for the purpose of planning and control at the national level. It must be pointed out, however, that the information needs of external users should be seen only as a small part of the overall objectives of the accounting system, let alone the situation in Saudi Arabia, where there is much doubt about the size of such users and their ability to understand published accounting information and use it effectively for decision-making (see chapter 9).

¹ The contents of both volumes were approved by His Excellency Minister of Commerce Decision Number 692 dated 28/2/1406H (1986).

It can therefore be stated that any development of accounting in Saudi Arabia, as a developing country, should not limit its efforts to accounting practice, in the form of setting accounting standards for external financial reporting which will only be used by a very small uninterested group. It must go beyond that. As Mirghani (1982, p.58), pointed out:

"In developing countries, the development of accounting should be viewed as equivalent to the development of part of the infrastructure necessary for achieving economic development. It is, therefore, imperative that specific frameworks for the development of accounting, along with certain dimensions, need to be established so that the ultimate objective of providing reliable information support for the economic development process can be reached."

Although Saudi Arabia has built one of the most modern economic infrastructures in the region, within a relatively short time, very little has been done to build its accounting system. More specifically, the researcher believes that the accounting system in Saudi Arabia is not adequate to provide sound accounting information on which users at both micro and macro levels can base rational decisions, for the prevailing system is based primarily on the legal and authoritative framework, together with the discretion of accountants.

1.2 Objectives of the study

One of the main shortcomings of the efforts carried out so far to develop accounting in Saudi Arabia, including the recent project supported by the Ministry of Commerce, was the great emphasis placed upon the accounting profession and external financial reporting. It should be pointed out, however, that the present unsatisfactory state of affairs cannot be blamed on these two accounting issues alone; it is the end product of a complicated causal system. Therefore, any programme of action aimed at making accounting a more useful tool in the economic development of Saudi Arabia must be based on thorough consideration of the problem as a whole, with all its components (education, profession, enterprise, government and national accounting). With this in mind, the present study is basically designed to accomplish the following objectives:

1. To determine the current status of the accounting education and the accounting profession, and the environmental factors affecting these two components (chapter 4-5).
2. To examine the prevailing accounting recording, classification and reporting procedures at both micro (enterprise and government) and macro (national) levels in Saudi Arabia, in order to find out whether they provide information relevance to the socio-economic environment (chapters 6-8).

3. To review and evaluate the new accounting and auditing guidelines which were introduced recently in Saudi Arabia (chapter 9).
4. To discuss the accounting information that is actually needed in Saudi Arabia, particularly for the construction and implementation of national development plans, and to show how such information could be best reported to the ultimate users. For example, would uniform accounting approach be of greater advantage than flexible approach in this respect? (chapter 10).
5. To draw the attention of the authorities and accountants in Saudi Arabia to the shortcomings of various accounting aspects, and to convince them that the best approach is to tackle such shortcomings simultaneously (chapter 10).

In order to accomplish the above objectives, it is necessary to review briefly the function of accounting in economic development, the status of accounting in developing countries in general, and the main approaches suggested for improving accounting in these countries (chapter 2). It is also necessary to examine the environmental characteristics (social, political, regulatory and economic) in which accounting operates in Saudi Arabia (chapter 3).

1.3 Significance of the study

There is an abundance of literature concerning accounting in developed countries, such as the UK, USA, and other western countries, but less has been found dealing with the subject in developing countries. Even the little that does exist is mainly written by western authors. Enthoven (1973, 1975, 1977, 1980, 1981) has perhaps done more than any other writer to draw attention to the deficiencies of accounting systems in developing countries and the major problems facing these countries in establishing accounting systems relevant to their socio-economic environment needs.

In his well-known book Accountancy Systems in Third World Economies published in 1977, Enthoven discussed the accounting problems of developing countries in Africa and Asia, the Asian countries covered being Hong Kong, India, Indonesia, Iran, Malaysia, Pakistan, Taiwan, Thailand, and the Philippines. "He also suggested ways of improving the revealed inadequacies in the accounting practices, institutions and education of these developing countries" (Wallace, 1990, p.8).

It can be seen that although Saudi Arabia is located in Asia, it was not included among the countries studied by Enthoven. Moreover, Saudi Arabia has not been included in any international accounting surveys carried out either by accounting organisations (e.g AICPA, 1964 and 1975) or by international accounting firms (e.g PWI, 1973, 1975 and 1979). This may be attributed, at least in

part, to the fact that Saudi Arabia as yet does not have a professional accounting body which could represent it in such international surveys, and to the language barrier.

In addition, to the knowledge of this researcher, no comprehensive research has been conducted to analyse and evaluate the accounting system and its components (education, profession, enterprise, government and national accounting) simultaneously with the socio-economic environment needs of Saudi Arabia.

So far, publications on accounting issues in Saudi Arabia, which have been presented for the attention of the international accounting literature, have been confined to a few articles (e.g. Abdeen and Yavas, 1985; Merei, 1985; Eikharouf, 1985; Moustafa, 1985; Abdelsalam and Satin, 1988; Abdelsalam, 1990) and some Ph.D theses in the United Kingdom and United States (e.g. Shanawi, 1970; Kordi, 1979; Ba-essa 1984). Most of the works of these researchers and academics dealt with the problems of the accounting profession, and ended with recommendations emphasising the development of this component along the lines of the UK/USA approach. Although Kordi (1979) studied the major characteristics of the accounting system in some selected Saudi industrial businesses, he seemed to show particular enthusiasm for the American accounting system, saying:

"In particular reference to accounting advancement in Saudi Arabia, the present author supports the idea that the Saudi Accountants

study and adopt the American accounting ideas. In other words, we should divert attention from the Egyptian and the British schools and concentrate primarily on studying the American accounting concepts."

With great respect to these authors, there is ample evidence to question the assumption that what might be good accounting for the industrially developed countries such as the UK and the USA will automatically be good for developing countries such as Saudi Arabia. This is because there are a large number of environmental differences between these two groups of countries, so that the experiences of the former may have little relevance for the latter. That is why a number of accounting scholars have argued that the evolution of accounting in developing countries may have to take place in a quite different atmosphere from that which exists in industrialised countries (Briston, 1978; Samuels and Oliga 1982; Perera, 1985; Belkaoui, 1988).

It would thus appear from the foregoing discussion that there is a notable lack of comprehensive studies concerning accounting systems in developing countries in general, and in Saudi Arabia in particular. The need for intensive accounting research in developing countries has been confirmed recently by Wallace (1990, p.44) when he stated that:

"There is an urgent need for a deeper understanding of accounting systems in developing countries. This need can only be fulfilled by intensive research of those issues peculiar to developing countries. ... The scope of accounting should not be limited to

financial reporting and professional status of accountants. There is an urgent need for research into public sector accounting of Third World, ... Little has been written on the state of management and social accounting and on the sociology of accountants in these countries."

The significance of the present study, therefore, lies not only in its comprehensive coverage of diverse aspects of accounting (e.g. education, profession, enterprise, government and national accounting) in developing countries, but also its consideration of different accounting systems (e.g. flexible and uniform) and the socio-economic environment needs of developing countries, as well as the main approaches suggested for improving accounting in these countries. An awareness and understanding of these issues is important particularly for a country such as Saudi Arabia, which is now in the process of developing its own accounting system. Although the emphasis here is placed upon the Saudi Arabian environment, it is hoped that other developing countries would benefit from this study, particularly, the GCC countries which have similar environments to that of Saudi Arabia. It is also hoped that this study will go some way towards filling the existing gap in the literature concerning the status of accounting systems in developing countries and contribute to greater understanding of their accounting problems.

1.4 Methodology of the Study

The present study is unique in that it covers diverse aspects of accounting in Saudi Arabia. Thus, its research methodology included two main approaches: theoretical analysis and empirical survey (questionnaires and personal interviews).

1.4.1 Theoretical Analysis

This part of the study was carried out to serve as an introductory background to the study, and involved the following:

1. Library research was undertaken to provide background information on the function of accounting in economic development, the status of accounting in developing countries, and the main approaches suggested for improving accounting in these countries.
2. Background materials were gathered on the social, political, regulatory and economic environment in which accounting operates in Saudi Arabia, with particular reference to the recent rapid changes in the Saudi economy and the effect of such changes upon the development of accounting. Several documents and copies of decrees, laws and regulations related to the economic and business environment were obtained from official sources in Saudi Arabia. All of these documents were in Arabic and had to be translated into English by the author. Some materials related to the Saudi environment were found in the Arab Gulf Studies Centre, University of Exeter, England. Two visits were arranged by the author for this purpose.

3. Data concerning accounting education were collected from secondary sources, including prospectuses, bulletins and reports of various institutions offering accounting education programmes in Saudi Arabia. These materials provided statistical data concerning the contents of the accounting education programmes, number of credit hours required for various degrees and number of students, graduates and teachers.

1.4.2 Empirical Survey

This survey was carried out to achieve the main objectives of the study, stated earlier. Field work was carried out in Saudi Arabia over a period of three months (November 1989 to January 1990). It involved two questionnaires sent to two subject groups, and personal interviews, as follows:

The first questionnaire (see Appendix A) was designed to reveal some vital aspects of current accounting practice in Saudi Arabia, for example: type(s) of accounting standards widely used by public accountants, reasons for such, types of accounting services rendered and public accountants' opinions concerning the recent accounting and auditing guidelines. This questionnaire was sent to a sample of 100 public accountants licensed to practise in Saudi Arabia, of which 86 replied. The results of this survey are analysed and discussed in chapter 5.

The second questionnaire (see Appendix B) was addressed to the financial managers of 25 Saudi

corporations operating under the industrial sector, which form 37% of the existing corporations as at the end of 1989. This sector was selected because it has always been given high priority in overall development plans and has a potential role to play in the economic diversification. The survey here concentrated on the main features of the accounting systems of these enterprises (e.g. the design of the accounting system, data processing method, chart of accounts, financial reports currently prepared, their frequency and their users); rules, methods of classification and reporting procedures; the extent of use of accounting techniques for planning and control purpose; relationship to national accounts; accounting manpower problems and other related issues. Responses received concerning these issues were analysed and discussed in chapter 6.²

Interviews were conducted with key government officials in the Ministry of Finance and National Economy, General Audit Bureau, National Accounts Department, and Ministry of Planning (see Appendix C for a list of interviewees). All the interviews were conducted in the headquarters of these ministries and departments in the capital, Riyadh, during the official working hours in the period from 2 to 31 December 1989. The aim of these interviews was to gather data concerning accounting recording, classifications and reporting procedures used in the public sector (chapters 7-8).

² Construction and distribution procedures of these two questionnaires are discussed latter in the applicable chapters.

Finally, data collected from the theoretical study and from the empirical works were analyzed, summarized and presented in narrative and tabular form as appropriate. Analysis focused upon the environmental characteristics (social, political, regulatory and economic) in which accounting operates in Saudi Arabia, the status of the accounting system and practices, the recent accounting developments, the socio-economic development needs, and how the overall accounting systems could be improved to better satisfy these needs.

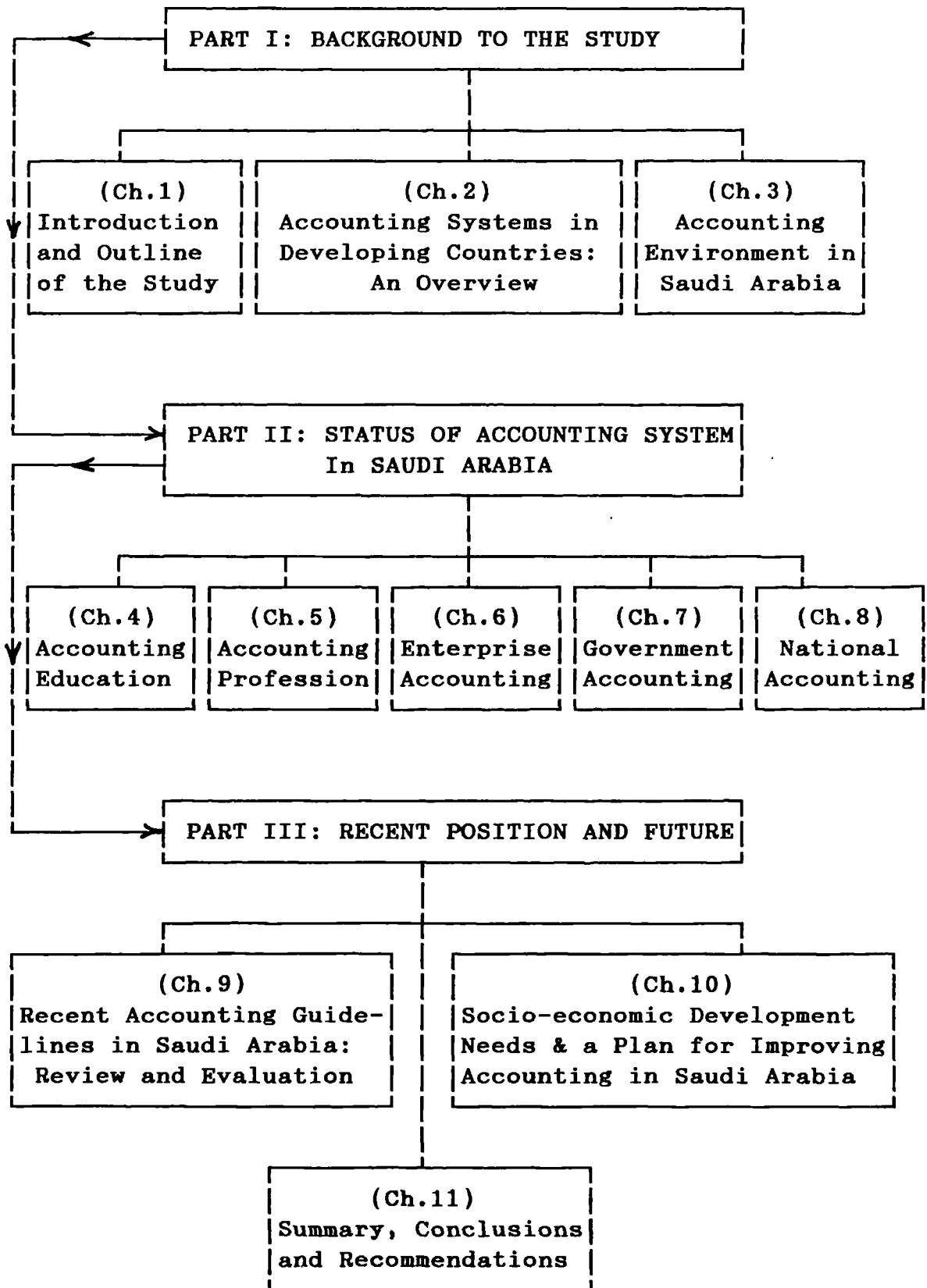
1.5 Outline of the Study

In his pioneering study concerning accounting in developing countries, Professor Enthoven (1973, p.308) argued that:

"In order to get a clear idea of the accounting requirements of each developing country or region, an assessment must be made of: (a) the environmental conditions of accounting, (b) the status of the branches and activities of accounting in the micro and macro economic spheres, and (c) the necessity and feasibility for improving all forms of accounting."

Thus, the present study is organised into three related parts with a total of eleven chapters (see figure 1.1) as follows:

Figure 1.1 Organization of the Study



Part I (chapters 1-3) is intended to provide a general background to the study. Chapter (1) describes the problem, objectives, significance, and methodology of the study.

Chapter (2) highlights the main characteristics of developing countries, the function of accounting in economic development, the status of accounting in developing countries and the main approaches suggested improving accounting in these countries.

Chapter (3) aims to provide the necessary background for the environmental characteristics (social, political, regulatory and economic) in which accounting operates in Saudi Arabia. The main changes in the accounting environment since 1970 are presented and analysed.

Part II (chapters 4-8) - Status of Accounting Systems in Saudi Arabia - presents a more or less comprehensive analysis and evaluation of accounting education, the accounting profession, enterprise accounting, government accounting and national accounting in Saudi Arabia.

Chapter (4) deals with accounting education in Saudi Arabia as the main source of the accounting manpower needed in the country. The discussion in this chapter focuses upon the accounting education programme both at pre-university and at the university level, accounting instructors, and teaching methods and techniques. Some problem areas in accounting education are also identified and discussed in this chapter.

Chapter (5) deals with the accounting profession in Saudi Arabia. Discussion in the first part of this chapter focuses upon how this component has developed and the factors which influence accounting practices. The second part analyses and discusses the empirical survey carried out in Saudi Arabia in order to contribute to better understanding of some practical aspects of prevailing accounting practices.

Chapter (6) examines the accounting recording, rules, methods of classifications and reporting procedures utilized by Saudi corporations with particular reference to the industrial sector.

Chapter (7) examines the current government accounting system in Saudi Arabia, with particular emphasis on the development of the general budget, its process and classification, closure of accounts and preparation of the final accounts of the state. The General Audit Bureau (GAB) and its function as an independent body responsible for controlling public funds is also discussed in this chapter.

Chapter (8) deals with national accounting in Saudi Arabia. The chapter focuses on the type of national accounts currently prepared in Saudi Arabia, the methods used, the users of the national accounts, problems concerning their construction and proposals for improvement.

Part III (chapters 9-10) discusses the recent accounting developments, socio-economic development needs of Saudi Arabia, and how accounting could be improved to better serve these needs.

Chapter (9) is devoted to the recent accounting standardisation programme in Saudi Arabia. The approach adopted together with the contents of the accounting and auditing guidelines established so far are reviewed and evaluated in the last section of this chapter.

Chapter (10) discusses socio-economic development in Saudi Arabia and the type of accounting information actually needed, particularly for the construction and implementation of the national development plans, development projects and Specialized Credit Institutions (SCIs); and how the uniform accounting system, if adopted, might facilitate the provision of this information. A proposed plan for improving the accounting system as a whole in Saudi Arabia is presented and discussed in the last section of this chapter.

Finally, the thesis ends with chapter (11), offering a summary and conclusions derived from the study. This final chapter also includes recommendations for further improvement of accounting in Saudi Arabia.

CHAPTER 2

ACCOUNTING SYSTEMS IN DEVELOPING COUNTRIES: An Overview

2.1 Introduction

The purpose of this chapter is to highlight the main characteristics of developing countries, the function of accounting in economic development planning, the status of accounting systems in developing countries and the main approaches suggested for improving accounting in these countries.¹ An awareness and understanding of these issues is particularly important for the discussion and analysis of the accounting system and practice in Saudi Arabia which are the main themes of this thesis.

The main part of this chapter, therefore, contains four sections: The next section explains what is meant by the phrase "developing countries". In section three, the function of accounting in economic development planning will be emphasised. This is particularly important as most of the developing countries, including Saudi Arabia, have adopted a comprehensive development planning approach as the principal means towards the achievement of accelerated growth. In section four, the status of accounting systems (education, profession, enterprise, government and national accounting) in developing countries will be briefly reviewed. In section five, the

¹ For a comprehensive literature review, see Dr. Wallace, R.S.O. (1990), "Accounting in Developing Countries: A Review of the Literature." In R.S.O. Wallace, J.M. Samuels and R.J. Briston (eds). Research in Third World Accounting, Vol. 1, pp.3-54. London: JAI Press.

approaches suggested for improving accounting in developing countries will be considered.

2.2 Characteristics of Developing Countries

No specific and generally used definition of the term, "developing countries" has been found in the literature. Other phrases such as "Third World Nations" and "Less Developed Countries" are used loosely in connection with these countries, which are "different in term of GNP, population, cultures, degree of literacy, economic and political systems" (Wallace, 1990, p.4).

It should be pointed out that some criteria have been used in the attempt to define developing countries. For example, the United Nations (1951, p.3) used per capita income and defined developing countries as "countries in which per capita real income is low when compared with per capita real incomes of the USA, Canada, Australia and Western Europe". However, this definition has been criticised on the ground that "in modern thinking, higher per capita income cannot be the only criterion to judge the level of development" (Talukdar, 1978, p.18). For example, Kuwait had in 1973-74 double the income level per capita of the United States, yet is still regarded as a developing country (Ibid).

For the purpose of his study on "Accounting and Developing Nations", Scott (1970, p.2) gave the following characteristics of these nations:

- (1) They are trying to experience the phenomenon of rapid economic growth, and many have had development programs for a number of years;

- (2) They are poor in economic terms, but are not the poorest nations;
- (3) They have potential for economic growth, and most are growing somewhat at present; and
- (4) Their economies do not have extensive or efficient industrial production but are thought to be in the process of transformation.

Chandler and Holzer (1984, p.453) pointed out that "although developing countries vary greatly in geographical size, population, access to natural resources, and degree of economic, social, and political development, they are generally identified by certain characteristics that they share in common". These include, among other things, unbalanced distribution of income and wealth; their exports usually consist of very few agricultural or mineral products; their domestic industries, although they are at varying stages of development, are on average rudimentary; most of them face serious balance of payment problems because their demand for imported goods far exceeds the foreign exchange earnings from their exports; very few enjoy stable democratic government; and the level of education of most of the population is low (Ibid., p.454).

In short, one might say that despite the differences in the terminologies used to describe developing countries, there is a general view that in many of these countries, social, economic, and political problems are the main concern of the people and authorities; as yet, accounting does not occupy a position of importance.

2.3 The Function of Accounting in Economic Development Planning

The traditional concern of the field of accounting has been to provide historical financial data regarding economic activities. However, in recent years the tendency has been to underline the economic decision-making function because of the utilisation of accounting data for planning and projecting future economic activities (Enthoven, 1977).

Further, the aspiration of developing countries in recent years to catch up economically with the developed industrial countries as rapidly as possible has been reflected in the adoption of the economic development planning approach as the principal means towards the achievement of accelerated growth. Saudi Arabia is no exception, socio-economic development planning is undertaken through consecutive five-year development plans. The first development plan started in 1970 and presently the government is half way through its fifth plan, which was launched in January 1990.

Accurate and timely information reflecting real economic conditions is essential for an effective planning process and for the effective economic development needed by any developing country such as Saudi Arabia.

Many consider that if national planning is used as a tool for achieving national development, then accounting should be attuned to the planning system to provide useful input material. Linowes (1969, p.18) pointed out

that the only way for planning in developing countries to be effective is through availability of adequate information for central planning. Ameiss (1971, p.90) stated that "accounting provides essential keys both to the measurement of available resources and to the control of their use. Since a nation seeking rapid development tends to rely on centralized national planning for the allocation of basic resources to stated national objectives, accounting can make a significant contribution to the achievement of such goals."

Enthoven (1973, pp.168-69) suggests the following contributions which accounting can make to development planning:

1. definition, classification, and valuation of transactions and stocks for all social accounts, in particular the national income and input-output accounts;
2. assessment of, and changes in, the components of input-output data, capital coefficients and shadow prices, the latter being the equilibrium or true prices of factors of production;
3. a uniform and standardized system of industrial accounts that would assist in obtaining more comparable data and coefficients for different countries;
4. up-to-date cost accounting procedures for cost-benefit calculations at various sector levels;
5. assistance in estimating future financial results and determining how these will affect investments and the planning pattern;
6. assistance in devising economic policies, measures, and programs; this may include help in elaborating tax or incentive provisions and other administrative policies to stimulate industrial growth;
7. control and audit of the plan, and reporting its results.

Seidler (1967, pp.1-2) examined accounting practices in Turkey and emphasised the relationship between accounting and economic development. He divides this relationship into two levels. First, consideration is given to the relationship of accounting - the skills and techniques which make up its body of knowledge - to certain elements of the development process. The second level of the study is the building of the body of required accounting skills. These skills are represented by a store of techniques which can be discovered and written down, and by a body of experienced manpower which may be difficult to transfer and also difficult to produce in the underdeveloped countries.

Shuaib (1980a) carried out a similar study and discussed the relationship between accounting and the development planning process of Kuwait. He cited certain areas in which accounting can facilitate the development planning process, such as the determination of the growth rate and the national income accounts, which are based, to a substantial extent, on accounting information.

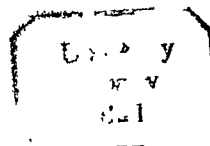
Cassell (1979, p. 23) highlights "an urgent need to recognise that accounting is a necessary technique for aiding economic development, particularly in Third World countries which are involved in economic growth and development... This will require the promotion of a new type of accountancy, called 'economic development accountancy'". He concluded that accountants are capable of: "(a) investigating development budget variances; (b)

determining whether project objectives have been met; (c) attesting to what the money has been spent on. Therefore the accountants do have an immediate role to play at the operational level of economic development, to perform cost benefit analysis (even of alternative programmes) and analyses of budgetary and other financial data".

Foroughi (1981, p.182) states that "accounting can help the economic and industrial development processes of developing countries in two ways: (a) by leading and guiding the investing parties to invest in useful, profitable and productive projects, and (b) by helping the management of the industrial and business enterprises to plan for the efficient utilization of development capital."

Both Enthoven (1977) and Belkaoui (1985), while recognising the positive contribution accounting could make to developing countries seeking economic development, considered that to be successful in this respect, the accounting systems of developing countries should conform to the national social, political, and economic settings; and be adaptable and useful to the national development plans.

It would thus appear from the foregoing brief discussion that accounting plays a significant role in economic development planning, and such role is likely to continue. This was confirmed recently by Hopwood et al (1990, p.39) in the following statement:



"Accounting is, has been, and no doubt will continue to be, intimately involved with the development of the economy as a whole. As one of the most important forms of operational economic calculation, accounting has not only reflected prevailing economic conditions but has also played a significant role in enabling the implementation of different strategies for the management of both the national economy and particular enterprises within it."

2.4 Status of Accounting in Developing Countries

For the purpose of this study, accounting is viewed as a system consisting of five components or subsystems (education, profession, enterprise, government and national accounting). Thus, this section is divided into five sub-sections each of which briefly deals with one of these components.

2.4.1 Accounting Education

The need for education and training to provide well-qualified accountants for developing countries has been developed over the past two decades (Scott, 1970; Enthoven, 1981). To improve the usefulness of accounting to developing countries, Scott (1970) argued that accountants in those countries should receive a liberal accounting education to enable them to view accounting and business enterprises in perspective as parts of the total social and economic structure.

Enthoven (1981) assessed the importance and function of accounting education, training and research in the context of socio-economic development management, with special reference to developing countries. His study

covered the following countries: Brazil, Egypt, India, Indonesia, Kenya, Korea, Libya, Malaysia, Mexico, Pakistan, Philippines, Somalia, South Pacific, Tanzania, Thailand, Venezuela.

Enthoven (1981) regarded the "soft spots" (weaknesses) in accounting education in developing countries to be a lack of specialized training in systems, controls and economic developmental accounting, in academic training; a lack of "in house" educational programmes in institutional training; and a paucity of institutions offering vocational and technical training for the development of basic skills.

In order to enhance accounting training and the profession, Enthoven (1981, p.38) advocated that accounting education should consider the following:

1. A conceptual socioeconomic foundation of accounting education and training.
2. A further specialization in the various branches of accounting.
3. A closer link among the institutional, professional, and educational programs and continuous education.
4. A greater focus on forecasting techniques, of both an internal and external nature.

Accounting education in developing countries has also been studied and assessed by some accounting bodies. For example, the AAA Committee on Accounting in developing countries (1976, pp.198-212) stated that the main educational problems in these countries are as follows:

1. Inadequacy of locally authored textbooks; local accountants most qualified to write are too busy to do so.
2. Inadequate teaching of accounting subjects at the college level. Accounting instructors in most cases hold several jobs to supplement their teaching salaries.
3. Lack of qualified instructors at the college level. There is a general shortage of accountants and educators.
4. Lack of professional development opportunities for accounting educators and practitioners
5. Inadequate accounting education for managers and prospective managers.

The Committee also mentioned other educational problems, of less importance, which include inadequacy of translated accounting texts, lack of translated accounting literature of advanced nations, poorly organised college educational accounting programs, and inadequate accounting libraries and other educational resources in colleges and universities (Ibid).

2.4.2 Accounting Profession

In developing countries, the accounting profession is either very weak or nonexistent. This would have adverse effects on these countries. Enthoven (1977, p.44), in reference to developing countries, stated that:

"The accounting profession also is considered inadequate to encourage and safeguard the investment of shareholders, owners and creditors in many countries. Investment in enterprises will be hampered if the (independent) external accountability role is weak. The investor consequently might be less interested in the earnings record than the dividend payment of a company, and companies might be forced to pay dividends even under

adverse circumstances to please shareholders. A side effect is that individuals often are unwilling to invest in their own area, due to a lack of adequate information, confidence and assurance that funds will be used properly. Consequently, capital formation and capital market functions may not be optimized."

The accounting professions of some developing countries are affected in one way or another by their colonial history. Briston (1978, p.113), for example, states with reference to Indonesia, that "the profession is Dutch in its qualification structure, but the training ... and philosophy are American. Neither, however, is in the least relevant to the needs of Indonesia, a country with no Companies Act, no capital market, a massive public sector, and an economic and cultural environment totally dissimilar to that of the Netherlands or the United States".

Wallace (1989, p.31) states that "A major problem facing accounting firms in Nigeria is the determination of competence limits for their particular practices. Only a few firms have more than two partners. These few are either those founded in Nigeria by international accounting firms or those pioneered by the few Nigerians who qualified before independence and have inherited British culture of accounting practice."

Enthoven (1980, p.76) describes some of the problems facing professional accounting in developing countries. He stated that "In Third World Countries ... no recognition may exist of the need for a professional institute to set standards for accounting and auditing,

codes of conduct, training and qualification tests. The institutional setup may suffer from insufficient professional interest, inadequate governmental encouragement and lack of support by private and public institutions."

Shuaib (1980b, p.87) describes the status of the accounting profession in Kuwait, which has a similar socio-economic environment to Saudi Arabia, as follows:

"The accounting profession in Kuwait has no statement of generally accepted accounting principles. Moreover, no code of professional ethics has been developed. Kuwait accounting practice is derived from the practices of the United States and Europe. So far nothing has been done to develop accounting principles and auditing standards and procedures suitable to the environment of the State of Kuwait".

Undoubtedly, some changes in the accounting profession in Kuwait have occurred since Shuaib's article. For example, at the beginning of 1987, the Ministry of Commerce and Industry issued three accounting statements. The point, however, remains valid, as each of these statements follows more or less the requirements of the related IASs published by the IASC which is dominated by UK and USA accountants.

Mcphail (1982, p.242) pointed out that "the present role of the profession in the developing countries varies substantially, both in terms of organisation and in the use made of its skills. In the Philippines, for example, the profession is well established and accountants play a leading role in the country's economy. In some countries,

such as in French-speaking Africa, organisation of the profession is in an embryonic stage".

Lowe (1967, p.358) perceives lack of progress in the accounting profession as being due to a shortage of highly qualified professional people. He adds that people in developing countries prefer to study engineering, law, or the physical science, which are more recognised fields of learning, even though such employment may not be attractive.

Very recently, Heffer (1991), who works as adviser to the Overseas Development Administration (ODA), pointed out that many developing countries have a professional accounting body but very few of them offer a national qualifying examination. That constraint, and those imposed by the scarcity of educational resources, cause gaps to remain between the demand for and the supply of accounting technicians and qualified accountants.

It thus could be inferred that accounting professional bodies in many developing countries either do not exist, or exist but are not properly active. As a result, the IASs have regularly been adopted by developing countries' professional bodies to fill the gap created by the failure of local professional bodies to develop accounting practices. However, it has been argued that this is not an adequate solution, as the IASC is dominated by members from the developed countries and has concerned itself with those countries' problems rather

than those of the developing countries (Briston, 1978; Samuels and Oliga, 1982; Perera, 1985, Belkaoui, 1988).

2.4.3 Enterprise Accounting

Enterprise accounting (i.e. financial accounting and managerial accounting) in developing countries suffers from many weaknesses, which make the information provided by the enterprise accounting system in these countries unreliable to a large degree. Enthoven (1977, p.44), in reference to developing countries, stated that:

"The amount of economically useful information generated by the enterprise accounting system for decision making often is scanty, unreliable, and untimely. Consequently, the system and its internal and external financial reports are not relied on to any major degree by investors, bankers, national statistical institutes, government or even management. Lending agencies are unable to get a clear picture of the status and performance of a company and greater reliance on proper collateral might be necessary in granting credit and loans."

Chandler and Holzer (1984, p.458) mentioned that a serious problem area for most of indigenous enterprises in developing countries concerns their in-house accounting systems, many of which are poorly designed and lack appropriate forms, procedures, and records.

Alhashim (1985, pp.4-7) pointed out that the published financial statements of companies in the Gulf region are far from informative, as these companies disclose little useful information to statement users, who have no access to additional information to enable

them to make informed judgements on financial positions and results of operations of the companies involved.

2.4.4 Government Accounting

The accounting systems in the public sectors of developing countries are no better than those of the private sectors. Government accounting is viewed as a control device for public receipts and expenditures. No focus is made on measures of efficiency, effectiveness, and economy of governmental operations (Enthoven, 1977, p.50). Enthoven (1991, p.268) stated that "accounting procedures [in government sector] often reflect such a complicated system of checks and balances that efficacy and timeliness are hampered."

The shortcoming of the governmental accounting systems in developing countries is reflected on the governmental budgetary process. The governmental accounting data, upon which budgets and plans have to be based are usually deficient, while budget items rarely assessed from a managerial (performance budget) point of view. Enthoven (1991, p.268) added that in developing countries:

"A tremendous gap sometimes exists between budgetary estimates and actual receipts or expenditures, and the budgetary audit may be performed long after the end of the fiscal period, when it no longer serves its purpose. Productivity appraisals may not be made at all. Auditing in the government sector tends to be a highly neglected and outdated procedure. As for economic planning, limited use is made of Accounting skills."

Dahmash (1982) in his study entitled "Public Auditing Development in the Arab States: A Comparative Study", which aimed to evaluate the existing Supreme Audit Institutions and their effectiveness in sixteen Arab states, including Saudi Arabia, concluded that, in recent years, the Arab states have placed more emphasis on implementing comprehensive national plans. The achievement of the goals and objectives of these plans, in addition to the maximization of the quality of various governmental services, has challenged the various national Supreme Audit Institutions to play a more effective role in conducting their audits. His study (p.109) indicates that:

"These institutions suffer from various problems, both internal and external. Internal problems include organizational structure, lack of full independence, lack of qualified staff, losses of qualified staff, lack of adequate training programs, and institution budget constraints. External problems result from rapidly changing economic, social, and political pressures, bureaucratic traditions, inadequate reporting, weak control, and insufficient information in audited units; however, there is also a lack of adequate coordination and integration of control systems with other financial control bodies".

Dahmash (1982) put forward suggestions for improving the effectiveness of the present national audit institutions in the Arab states in order to play a more effective role in the process of auditing and evaluation of government units and development programmes. His recommendations included, among other things, the

adoption of a comprehensive auditing approach which embraces three levels (a) financial and compliance; (b) economy and efficiency; and (c) programme results. This approach is based on the generally accepted auditing standards adopted by the U.S. Government Accounting Office (GAO).

Another example for the deficiencies of government accounting in developing countries was given recently by Wallace (1989) with reference to Nigeria. He pointed out (p.19) that "Government financial reporting is either non-existent or totally inadequate. ... Whether at local, state or federal level of government, published financial statements do not present to their readers a comprehensive picture of government operations expressed in financial terms. Often, government financial reporting is limited to statements or listings of actual revenues and expenditures compared to appropriations."

2.4.5 National Accounting

In many developing countries, national accounting and its system of classification have progressed fairly adequately. The major obstacle is the lack of reliable accounting data from the private and public sectors of these economies. Enthoven (1973, p.62) stated that:

"Macro accounting has progressed fairly adequately in many developing countries; the system of classification (into sectors, accounts and transaction) and the procedures used may be quite well reflected. But, when information from governmental and enterprise accounts is needed in the preparation of macro

accounts, tremendous gaps occur. One particular problem involves methods of quantifying and evaluating such data."

Enthoven (1973, p.32) attributes the inadequacies and the unreliability of national accounts in developing countries to poor financial accounting reporting practices. Briston (1978, pp.117-18) attributes them to western domination over accounting education and the accounting profession in those countries. He pointed out that most of the questions related to the needs of national accounts and development planning have never been considered in the UK.

2.5 Approaches Suggested for Improving Accounting in Developing Countries

The foregoing brief discussion shows that the overall accounting systems (education, profession, enterprise, government and national) in developing countries suffer from various problems and deficiencies. With these in mind, various approaches have been suggested for improving accounting in these countries. Wallace (1990, p.39) has grouped these approaches into four main categories. These approaches together with "A Systems Approach to Accounting in Developing Countries" suggested by Holzer and Chandler (1981) will be reviewed in this section. The review here focuses upon three basic elements: (a) the main theme of the suggested approach, (b) its implementation requirements and (c) arguments raised against it.

2.5.1 Scott Approach-EEvA

The first approach was suggested by Professor Scott (1970) and is referred to as "Economic Evaluation Accounting" (EEvA). This approach "requires the structuring of accounting so as to provide information to facilitate the economic evaluation of enterprises and the activities of managements, investors, and the government". The basis of this approach is to ensure that accounting information should provide maximum economic utility for users in developing countries and should be based solely on general economic principles of both a micro and macro economic nature rather than on business practice, accounting conventions, tax or other narrowly conceived legislation (Scott, 1970, p.149).

EEvA framework consists of two main parts: the first part examines the various functions - internal and external policy reporting for private and public enterprises - which accounting in developing countries should serve. The second part deals with key elements or factors which should be present for accounting to fulfil these functions. These key elements are current value measurement, education of accountants, legislative control and regulation of accounting, and professional aspects of accounting (Ibid. p.150).

The implementation of EEvA requires (a) a liberal arts-based curriculum; (b) a "fresh start" approach based on the standards of accounting education, practices and professionalism; and (c) establishment of small

programmes for a few carefully selected students, with gradual expansion as demand increases (Tipgos, 1987).

The main argument against the EEvA concerns its emphasis on the economic development of the Third World countries as the overriding objective of accounting in such countries (Tipgos, 1987; Wallace, 1990).

2.5.2 AAA Approach-EDA

The second approach was that recommended by the AAA Committee on International Accounting Operation and Education of the American Accounting Association. This approach is called "Economic Development Accounting" (EDA) and is based on three fundamental assumptions as follows:

1. Application of existing and potential accounting systems, techniques, procedures, and data to enhance economic development within a nation or nations.

2. Integration of all branches of accounting to serve effectively both micro and macro socio-economic decision-making.

3. Linkage of model educational modules required for economic development which demands: (a) A conceptual socio-economic foundation of accounting education and training; (b) Specialization in various areas of accounting; (c) Closer linkage between institutional, professional, and educational programs; and (d) Greater focus on forecasting techniques, both internal and external.

Implementation of the EDA is dependent upon the successful completion of two important requirements (AAA, 1977, p.88):

1. Inventory or "stock-taking" of quality of accountants, the available manpower, and the educational functional development in accounting areas.

2. Development of an accounting development plan to serve as a blueprint for implementing the model.

As with EEvA, the AAA-EDA approach is criticised for assuming that the overriding goal of accounting in developing countries is the economic development of those countries (Tipgos, 1987; Wallace, 1990).

2.5.3 Needles's Approach-TAT

Needles's approach is based on the proposals advanced by various accounting writers who argued that accounting in developing countries can improve through transfer of accounting technology (TAT) by designated transfer agents such as multinational corporations, transnational accounting firms, the United Nations, and other international or regional agencies (Lowe, 1967; Seidler, 1969; Enthoven, 1973).

Needles (1976) provides a most comprehensive conceptual framework by which a country may formulate a strategy for the international transfer of accounting technology as part of its overall economic plan. The proposed framework for the international transfer of accounting technology is presented in figure 2.1. In it, national goals combine with the social, political, and

economic environment and general resources and constraints to influence the overall economic plan. The economic plan itself contains, as a sub-plan, a strategy for the transfer of accounting technology, composed of objectives for the accounting technology transfer, strategy, channels of transfer, and levels of accounting technology.

The channels identified for purposes of this framework are as follows:

C1 - education institutions:

C11 - internal educational institutions;
C12 - foreign educational institutions;

C2 - international organisations;

C3 - government agencies;

C4 - multinational companies;

C5 - international accounting firms;

C6 - local companies; and

C7 - local accounting firms.

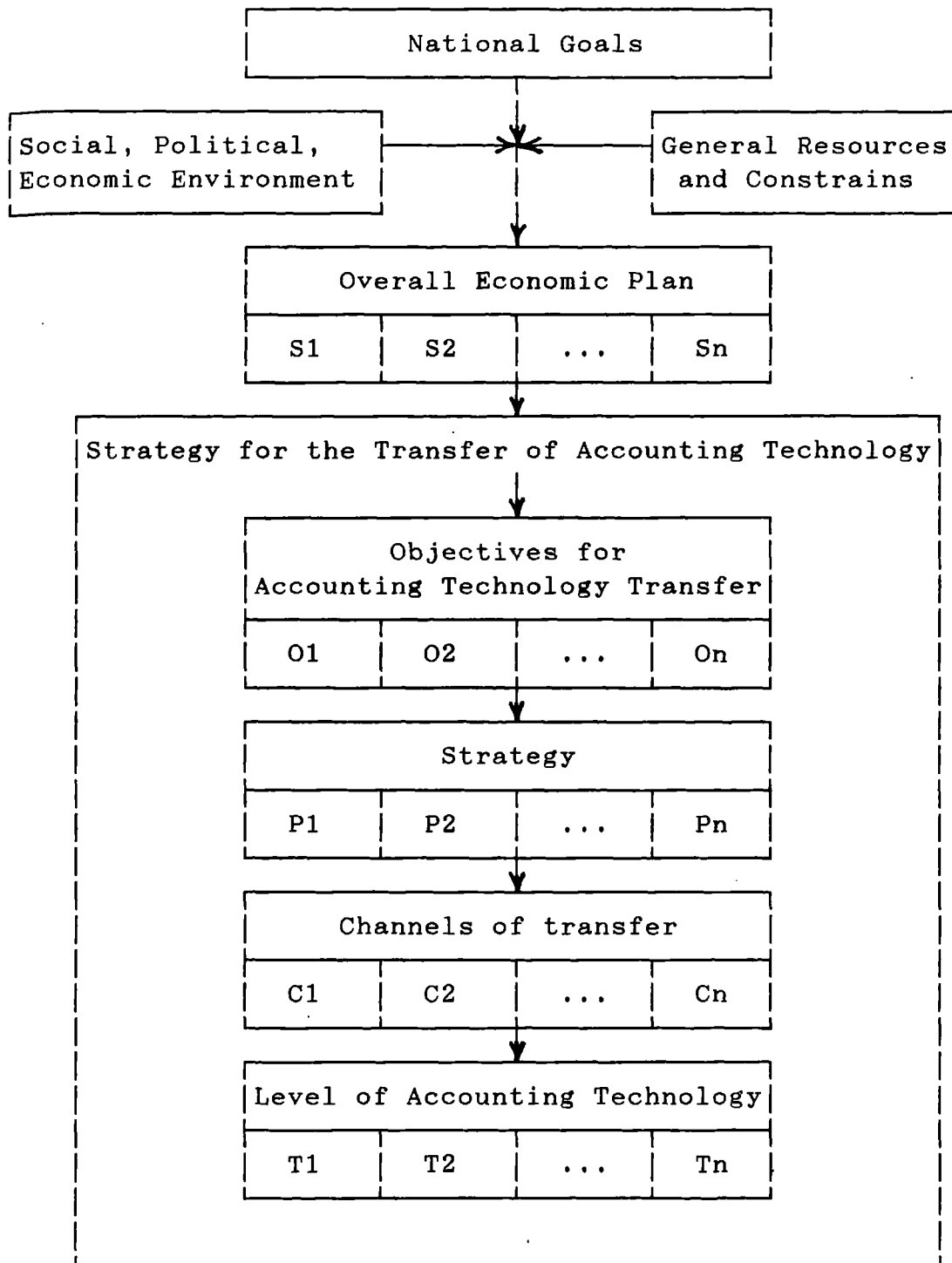
These channels, in turn, affect the levels of accounting technology in a country. The three types of technology, individual, organizational, and independent professional, are defined as follows:

T1 - level of technical accounting knowledge possessed by individuals;

T2 - level of sophistication of accounting techniques used by government and business organisations; and

T3 - level of advancement of an independent accounting profession.

Figure 2.1
 Framework for the International Transfer
 of Accounting Technology



Source: Needles, JR, B.E. (1976), "Implementing a Framework for the International Transfer of Accounting Technology," International Journal of Accounting Education and Research, Vol. 12, p.49

Implementation of the framework for the transfer of accounting technology to a developing country requires three separate and distinct phases. Each is designed to answer a different question concerning technology transfer, and each has different research characteristics. The three phases are:

"Phase I - Diagnosis. Diagnosis is descriptive and theory building in nature. It answers the question: What is? Research in this category has two tasks. One is the assessment of the existing levels of technology, the availability of transferable technologies, and the current state of the channels of transfer. The second, and equally important, task is to explain and provide a basis for predicting the behaviour of individuals and organisations involved in the technology transfer process in and for developing countries.

Phase II - Prescription. Prescription is normative in nature and answers the question: What ought to be? This activity has the task of setting levels and priorities of objectives and selecting appropriate accounting technologies and channels of transfer.

Phase III - Strategy Formulation. Strategy formulation is action-orientated and answers the question: How? It is the detailed technical task of devising policies and guidelines for legislation and other decision-making authorities which are compatible with the research findings in Phase I and will achieve the priorities set in phase II."

Several arguments have been made against this approach. For example, it is argued that while the mere transfer of accounting technology may appear to be of direct benefit to the developing countries, there is the cost associated with (a) the transfer of the wrong or inapplicable technology, (b) the lack of appropriate infrastructure for the correct application of the technology, (c) the increased dependence on outside experts, (d) the lack of incentives for developing local standards, and (e) the horrible loss of pride by some culture groups (Belkaoui, 1988).

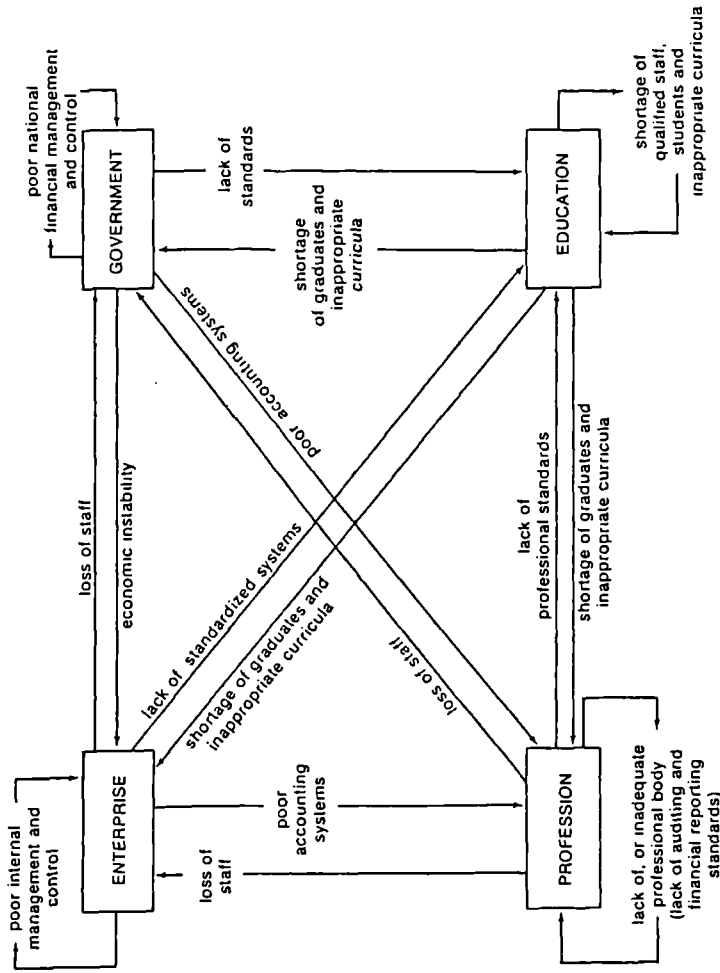
It is also argued that this approach may result in an inevitable transmission of some aspects of accounting principles and practices from advanced nations to developing nations in which those rules and practices may not be suitable (Amenkhienan, 1986; Hove, 1986).

2.5.4 Holzer and Chandlers' Approach-SA

Holzer and Chandler's (1981) approach is based on the "System Approach" (SA) to accounting problems in developing countries. According to this approach, accounting in developing countries is considered as an establishment consisting of four components: the accounting function in indigenous enterprises, the local accounting profession, the accounting function of government agencies, and the teaching of accountancy in educational institutions. The accounting establishment is viewed as a system and its constituent components are interrelated, such that the behaviour (including

Figure 2.2

A Systems View of the Accounting Establishment in Developing Countries



Key: A → B → C Component A causes Problem B for Component C

Source: Holzer, H.P. and Chandler, J.S. (1981), "A Systems Approach to Accounting in Developing Countries", Management International Review, Volume 21, p.28.

problems) of one component affects the behaviour of the others. The accounting problems which have been identified in each component are similar to those discussed earlier in this chapter.

Analysis from the system viewpoint yields two common, underlying problems: lack of qualified personnel, and ineffective accounting systems. A system view of the accounting problems in developing countries is presented in figure 2.2. Each of the four components is shown to have a significant effect on the other three.

Holzer and Chandler (1981, p.27) indicated that "developing countries attempt to solve the problems of each of the components independently. These efforts have led to only limited progress." A system solution is suggested whereby these underlying problems are attacked, through accounting curricula changes and professional standardisation, in order to facilitate the solution of the more visible problems.

Holzer and Chandlers' Approach-SA can be criticized for not considering national accounting as a component of the accounting system in developing countries, despite the fact that national accounting is particularly important because most developing countries have adopted a comprehensive planning approach which requires a great deal of information, most of which is expected to be supplied by national accounting.

2.5.5 Tipgos' Approach- TES

The Tipgos (1987) approach is referred to as "Two-Tiered Education System" (TES) which combines a paraprofessional and professional training for accountants in Third World countries. The first tier would be a two to three year paraprofessional course designed to equip the student with essential basic accounting skills relevant to the stage of development and needs of the country. The second tier would last for two to three years and serve as a continuation of the first tier. At both levels, the graduate could seek professional certification as administered by an appropriate body. The TES for improving accounting education in developing countries is presented in figure 2.3.

Tipgos' approach is based on the following main assumptions:

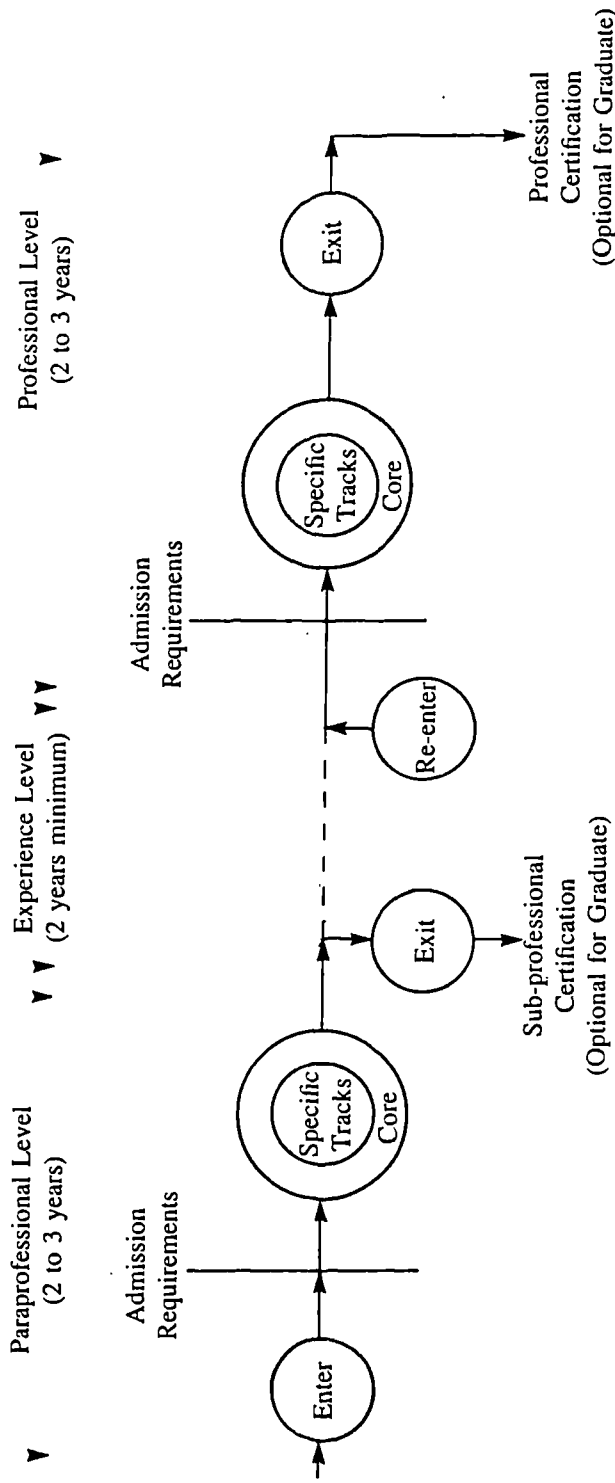
1. Economic development is a concerted and coordinated effort of all social institutions, of which accounting is considered one.

2. The accounting profession in developing countries has certain higher level aspirations not just economic development of the country.

3. Any plan to improve accounting in developing countries must provide for improvement in both accounting education and practice.

Figure 2.3

Two-Tiered Education System (TES)



Source: Tipgos, M. A. (1987), "A Comprehensive Model for Improving Accounting Education in Developing Countries." In Advances in International Accounting, Volume 1, K. Most (ed.), Greenwich, Ct: JAI Press, p.398.

4. Any form of assistance to improve accounting must be offered and implemented based on the three propositions above.

The implementation of the TES depends upon the level in question. According to Tipgos (1987), implementation at the paraprofessional level can easily be superimposed on the existing 2-year or diploma programmes common in certain developing countries. The implementation of professional level requires the definition of the overall objectives and sub-objectives of accounting in developing countries, as well as "accounting inventory-taking".

Tipgos (1987) suggests several advantages of TES, two of which are vital to its success. The first is the ease and flexibility of implementing the system. The second advantage is that it provides for both short-run and long-run accounting manpower needs of developing countries without dictating what ought to be the objectives of accounting in developing countries.

2.6 Summary and Conclusion

In this chapter, a general overview was given of the status of accounting in developing countries. The emphasis was on the main characteristics of developing countries, the function of accounting in economic development planning, the common problems of each individual component of the accounting system in developing countries and, above all, the main approaches suggested for improving accounting in these countries. These approaches include Scott's Approach-EEvA, AAA's

Approach-EDA, Needles's approach-TAT, Holzer and Chandlers' Approach-AS, and Tipgos' Approach-TES.

It was found that all these approaches appear to have similar objectives, i.e. to improve the accounting systems in developing countries. However, the first two approaches were criticized for their assumption that the overriding objective of accounting in developing countries is the economic development of those countries. The third approach was criticized because of the costs associated with the transfer of technology and an inevitable transmission of some aspects of accounting principles and practices from advanced nations to developing nations in which those rules and practices may not be suitable. The fourth approach seems to exclude national accounting as a component of the overall accounting system. Finally, the fifth approach concentrates on accounting education and professionalisation.

Furthermore, these approaches are aimed at developing countries in general, that is to say they are not directed to satisfy the specific needs of an individual country. Indeed, it can be argued that what developing countries need are systematic and carefully planned accounting systems designed to meet the unique needs of the individual country's accounting and socio-economic environment.

CHAPTER 3

ACCOUNTING ENVIRONMENT IN SAUDI ARABIA

3.1 Introduction

Accounting does not exist in a vacuum but interacts with an existing environment. Each country has its own unique social, political, legal, and economic environment which should play a significant role in shaping the accounting system.

An examination of the environment of accounting in any country should thus precede the study of its accounting system. Alhashim and Arpan (1988, p.9) emphasised this point:

"to understand properly any country's accounting system, one must understand the country's environment. This situation is true even for properly understanding the accounting of one's own country."

There are various environmental factors - social, political, legal, and economic - likely to influence the accounting system in any country. This influence has been discussed and investigated by many accounting authors. For example, Zeff (1972) demonstrated that the development of accounting principles comes from integration between theory, practice and social, economic and political influences. Arpan and Radebaugh (1985, 13-40) discussed some environmental characteristics that may be considered in studies of comparative systems of accounting, namely educational, cultural, legal, political, and economic factors. They regarded the last

group, economic factors, as the most influential, because they not only affect accounting directly, but also have substantial indirect effects on other environmental areas such as sociocultural attitudes, legal, political and educational objectives, which in turn affect accounting practices.

Chambers (1966, p.6) argued that the foundation of accounting "... is not the overt features of existing rules but the features of the environment in which possible rules are to apply". Moreover, Chetkovich (1972), emphasising the relationship between accounting and its underlying environment, noted that accounting in each country should develop only in a manner relevant to the society in which it exists.

Accordingly, the main purpose of this chapter is to provide the necessary background for understanding the characteristics of the environment in which accounting operates in Saudi Arabia. This basic background is important, particularly for readers in the Western World, where this thesis is written, since many of them may know little of Saudi Arabia except its main product, crude oil.

This chapter is based on official documents, reports, and articles which have been collected by the author from various sources, most of which were in Arabic and had to be translated into English by the author.

3.2 Social Framework

3.2.1 Geographical Profile

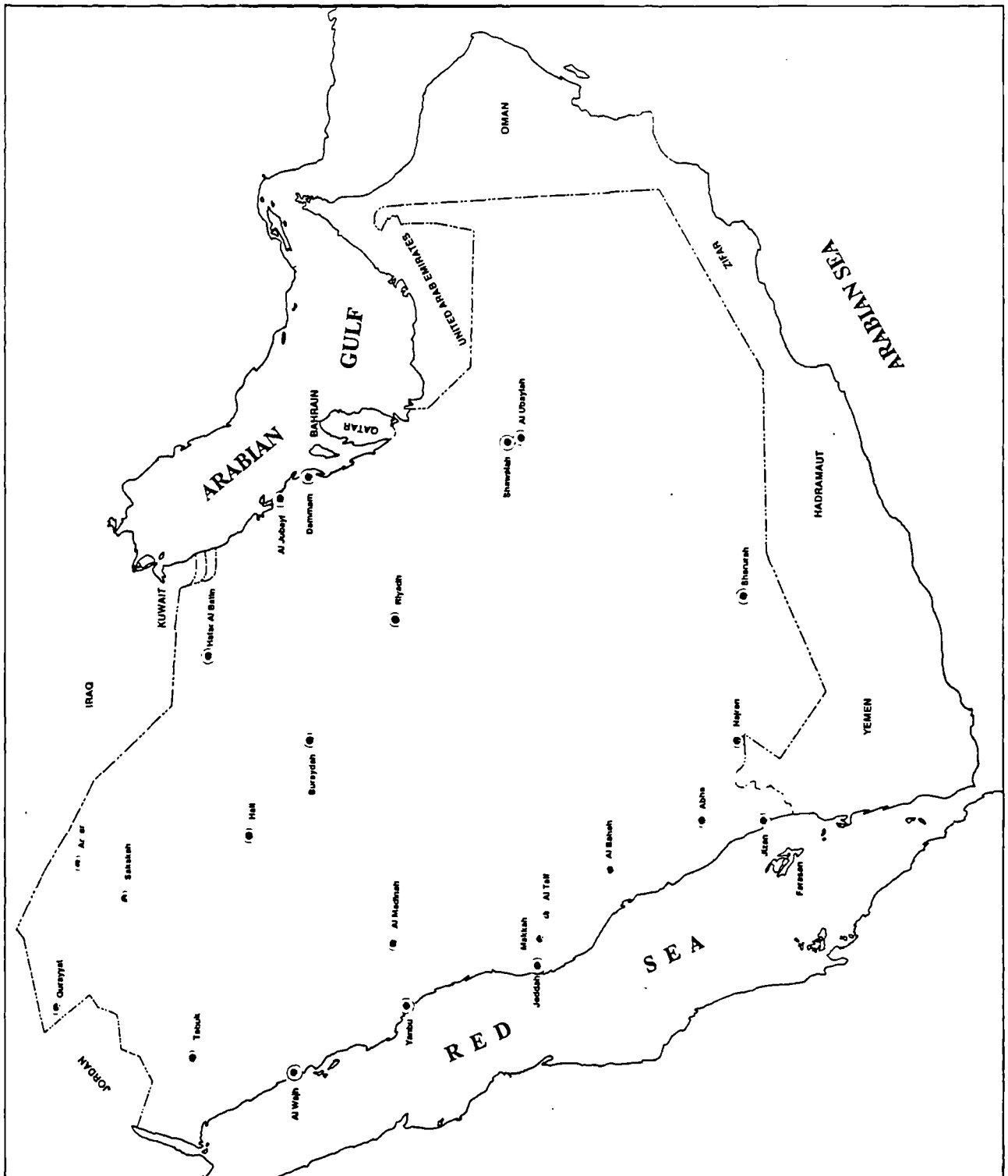
The Kingdom of Saudi Arabia covers a very large area, occupying four-fifths of the Arabian Peninsula, which is located in southwestern Asia. Its total area is about 2,240,000 square kilometres (over 870,000 square miles), nearly one-third the size of the United State of America or about ten times the size of the United Kingdom. It is the largest country in the Arab World and the twelfth largest globally (MEED, 1983, p.1).

The Kingdom is bounded to the north by Jordan, Iraq and Kuwait; to the east by the Arabian Gulf, Qatar and United Arab Emirates; to the south by Oman and Yemen; to the west by the Red Sea and Gulf of Aqaba. The geographical location of the Kingdom gives it strategical importance since it is considered as a bridge between the West and Asia (see figure 3.1).

Saudi Arabia is characterised by a mild climate prevailing over its various regions. On the whole, rainfall over Saudi Arabia is scanty since it falls under the influence of the sub-tropical high pressure system. Winter is moderately cold and dry. In summer, temperature increases considerably, accompanied by humidity in the coastal regions (Statistical Indicator, 1986).

Administratively, the Kingdom of Saudi Arabia is classified into five planning regions: the central region (Najd) contains the capital Riyadh which is the administrative centre of the Kingdom. It is the location

Figure 3.1 Kingdom of Saudi Arabia



Source: The Fifth Development Plan (1990-95).

of all the ministries, foreign embassies and the headquarters of the Gulf Cooperation Council (GCC).¹

The eastern region (Hasa) contains Alkobar, Jubail, Hafuf, and the port city of Dammam. This region is the location of the enormous oil-fields, the main source of the Kingdom's economic development, which extend from the Kuwait border in the north to the border with the United Arab Emirates in the south.

The western region (Hijas) contains the two Holy cities of Makkah and Medina which attract about two million pilgrims each year, the main Red Sea port of Jeddah, which is considered the commercial centre of the Kingdom, and the summer capital of Taif.

The southwestern region (Asir) is located along the southwestern coast of the Red Sea, between the Hijas region and the Yemeni border. This region is a mountainous region, much of which lies above 2,000 meters. Abha is the largest city and serves as the region's administrative centre.

The northern region extends from Gulf of Aqaba along the Jordanian border to the Iraqi border in the north. Nufud (the second largest desert in the Kingdom) occupies most of the region's surface. Tabuk and Hail are the two major cities in this region.

The Kingdom is further divided into fourteen Amirates, each of which is in turn subdivided into sub-

¹ The GCC was established in 1981. It consists of six Gulf countries. They are: The Kingdom of Saudi Arabia, State of Bahrain, State of Kuwait, State of Qatar, State of Oman, and the United Arab Emirates (U.A.E.).

Amirates. Each region, Amirate and sub-Amirate constitutes a planning unit (4DP, 1985-90, p.419).

3.2.2 History

The earliest urban settlements are believed to have developed in the southwest of the Arabian Peninsula in the 12th century B.C. and in the area's early history, it comprised a number of small trading centres surrounded by vast tracts of territory, roamed over by nomadic tribes. By the end of the sixth century A.D., the Hejaze cities of Taif, Makkah and Medina in the west had become prominent. Makkah, the birthplace of the Prophet Muhammad (PBUH), and Medina, the place of his burial, have retained a unique status as the centre of pilgrimage for the Islamic World.

The modern history of Saudi Arabia may be traced back to the early decades of this century. This phase began in 1902 when King Abdul Aziz (commonly known as Ibn Saud) recaptured the city of Riyadh and extended his power over most of the Arabian Peninsula. By 1932 he had unified all parts of the country under the name of "Kingdom of Saudi Arabia".

King Abdul Aziz ruled until 1953 when he was succeeded by his son, King Saud. In 1964, King Faisal became the third of the modern Kings of Saudi Arabia. In 1975, King Khalid succeeded his brother, King Faisal. On his death in 1982, he was succeeded by King Fahd, the present King, who also acts as Prime Minister.

3.2.3 Religion

Islam is the only religion practised in Saudi Arabia. The Arabic word Islam means peace, submission and obedience. The essence of Islam is found in the Qur'an which emphasises equality among people, tolerance of other religions and submission to the will of God. The Qur'an lays down rules and regulations for behaviour in private, social and business life. In fact, Islam is not a new religion. It is, in essence, the same message and guidance which God revealed to all his Prophets:

"Say: we believe in God and that which was revealed to us, and that which was revealed to Abraham and Ismail and Isaac and Jacob and the Tribes and in that which was given to Moses and Jesus and to the Prophets from their Lord; we make no distinction between one and another among them, and to God we submit." [The Holy Qura'n, Sura III, verse 84].

There are five basic "Pillars of Islam" which every Muslim must perform. The five Pillars are:

1. To acknowledge the absolute oneness of God and Muhammad as the messenger of God;
2. To pray five times daily within certain time limits and according to prescribed set rituals;
3. To pay Zakat (Religious Tax) to the needy and poor;
4. To abstain from all food, drink, tobacco, and sexual intercourse between sunrise and sunset during the holy month of Ramadan; and

5. To make a pilgrimage to the holy city of Mecca at least once in a lifetime, if financially and physically able.

Starting from these five pillars, Islam proceeds to direct the entire life of the follower by means of the Qura'n and Sunah. The Qura'n is the last revealed Word of God and the basic source of Islamic teachings and laws. The Sunah is the teachings, sayings and actions of the Prophet Muhammad, meticulously reported and collected by his devoted companions, which explain and elaborate the Qura'nic verses.

3.2.4 Language

Arabic is the official language of Saudi Arabia. English is the only foreign language taught in schools, starting from the intermediate level. Most of the government's officers and businessmen are fluent in English, particularly those who have received part of their education or training in the West.

In a recent circular, the government emphasised the use of the Arabic Language in drafting documents, such as contracts, as well as in effecting all correspondence between governments or agencies and foreign companies or their branches operating in Saudi Arabia. It also required companies to submit their accounts and statements to the Department of Zakat and Income Tax (DZIT) in Arabic and to maintain locally in Saudi Arabia all their books of account and records in Arabic (Circular No. 7533/6).

3.2.5 Population and Employment

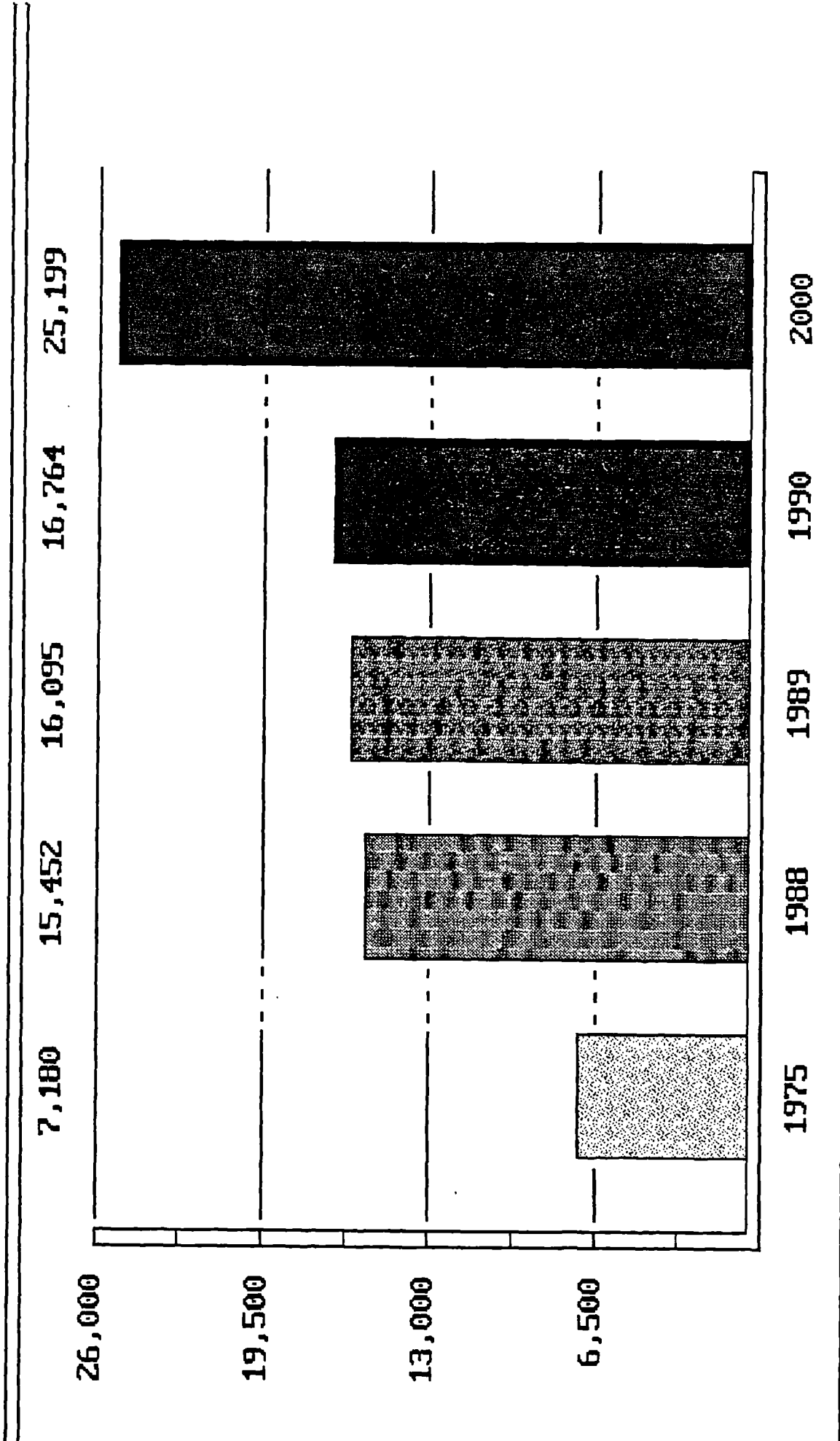
The human resources element is very significant for the economic development of any country as a whole and for accounting development within that country. This is because in many cases it is much easier to import capital from abroad rather than importing human resources. Hence, the study of population as a source of the skills required for the country is a major ingredient of the background information for this study.

The population of Saudi Arabia is small compared with the country's physical size. There are no exact population figures at the present time.² However, a recent edition of a software computer programme (PCGlobal, 1990) estimates the size of the total population of Saudi Arabia to be 16,764,000 in 1990. According to this programme, the annual population growth is 4.16%, population density is 7 inhabitants/sq km, and the population doubling time is 17 years. It also estimates that the population will reach more than 25 million by the year two thousand (see figure 3.2).

Most people are concentrated in the major cities, particularly Riyadh (the capital) and Jeddah (the commercial centre and the main sea port in the Kingdom). The remainder of the country is less populated. In some parts of the country the population density is less than one person per square kilometre. Certain parts of the

² It should be noted that a national census was planned to take place in 1991. However, it was postponed due to the recent crisis in the region and according to a government official, the beginning of 1993 will be the new date.

Figure 3.2 Saudi Arabian's Population (in thousands)



country remain almost totally uninhabited, for instance, Al Rub Al Khali (the empty quarter) in the south of the Kingdom, and Nofud desert within the northern region.

As far as employment is concerned, the official statistics show that the population has a low rate of participation in the civilian labour force. In 1989/90, the participation rate was 29.9% (Fifth Plan, 1990-95, p.125). One factor which might have contributed to this low participation rate is the limited opportunities for female participation; their participation rate in 1989/90 was only 5.5% (Ibid). However, the Fifth Plan has recognised this problem and hence introduced three policies to enhance the participation of Saudi women in the development of the Kingdom: preparation of an annual Saudization plan to increase gradually the employment of Saudi women in the public sector; periodic review of the occupations, in both public and private sectors, in which employment of women is deemed to be in accordance with the Sharia; and study of the feasibility of allowing women to teach boys up to grade four at the elementary school level (Ibid, p.131).

The Fifth Plan states that despite reduced economic activity during the Fourth Plan period, employment increased at an average annual rate of 1.9 percent. Table 3.1 shows the distribution of employment among economic activities for 1984/85 and 1989/90. The construction sector reduced its work force by nearly 12% over the Fourth Plan years. This reduction, however, was more than

offset by significant employment increases in community and personal services, and in the trade sector. Moderate changes in employment occurred in most other sectors of the economy. Government employment, however, grew at an average annual rate of 5.9 percent (Fifth Plan, 1990-95, p. 31).

Table 3.1
Employment By Sector in the Fourth Plan 1984/85 - 1989/90

Sectors	Employment				Average Growth Rate (%)
	1984/85		1989/90		
	(000)	(%)	(000)	(%)	
1. Producing Sectors					
Agriculture	538.0	10.3	569.2	9.9	1.1
Other Mining	4.2	0.1	3.5	0.1	(3.6)
Manufacturing	424.1	8.1	374.9	6.4	(2.4)
Public Utilities	112.2	2.1	126.9	2.2	2.5
Construction	1470.0	28.0	944.1	16.4	(8.5)
Sub-total	2,548.5	48.6	2,018.6	35.0	(4.6)
2. Service Sector					
Commerce	688.7	13.1	898.3	15.6	5.5
Transport & Commun.	316.5	6.0	262.3	4.5	(3.7)
Finance, R. Estate	130.0	2.5	99.0	1.7	(5.3)
Other Services	1,033.1	19.7	1,822.0	31.6	12.0
Sub-total	2,168.3	41.3	3,081.6	53.4	7.3
3. Government *	469.1	9.0	624.8	10.8	5.9
Non-Oil Sectors(1+2+3)	5,185.9	98.9	5,725.0	99.2	2.0
Oil & Natural Gas	58.7	1.1	46.8	0.8	(4.4)
Total	5,244.6	100.0	5,771.8	100.0	1.9

* Excludes non-civilian employment and includes daily wage workers not classified as civil servants.

Source: Ministry of Planning, the Fifth Development Plan (1990-95), p.32

3.2.6 Other Social Aspects

Economic and social development are interrelated and mutually reinforcing. The Fifth Plan (1990-1995) recognised this fact and hence appropriated 66.1 billion Saudi Riyals (16.8%) for health and social development, representing an increase of 11.5% from the Fourth Development Plan.

Saudi Arabia has pursued a policy which provides free health care services for the whole population. The Fifth Development Plan (1990-95) emphasised primary health centres programmes which have been introduced in recent years as the basis of integrated health services throughout the Kingdom. The Government allocated 52 billion SR for the health services during the Fifth Plan.

Beside the emphasis on health care, the Fifth Plan listed many social elements for development, for example, social affairs, social security, social care, social insurance and youth programmes and services. The main objectives of all these programmes are to compensate existing social imbalances, to improve living standards and the quality of life of the population, and to stimulate citizen participation in community development activities.

3.3 The Political System

The Kingdom of Saudi Arabia is a Muslim state. The teachings of Islam provide the basic foundation for daily life and government policy in the Kingdom. Its constitution is the Qura'n (i.e. Muslim Holy Book) and

Sunah (i.e. sayings and actions of Prophet Muhammed, peace be upon him) and all decisions of the government are guided by them. In defining the Saudi political system, Al-Amri (1982, p.12) states that:

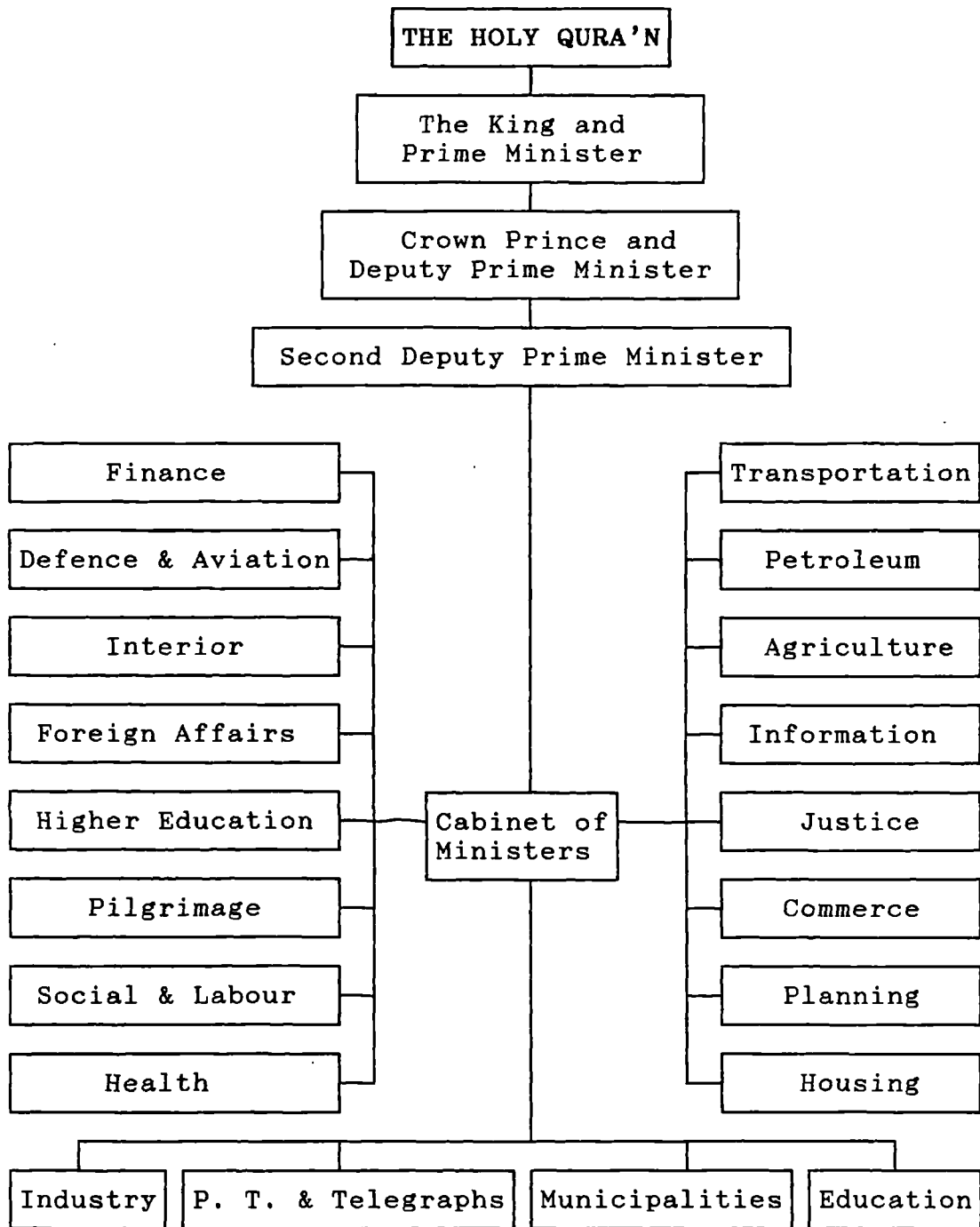
"One must realize that the system itself is not an absolute monarchy, as has been superficially judged. Saudi Arabia is not a secular state; it is an Islamic state. The Holy Qura'n forms the basis of all laws and no one, least of all the King, is immune from its precept."

There are no political parties or unions in Saudi Arabia. The government consists of the King, who acts as Prime Minister, the Crown Prince, who is also the Deputy Prime Minister, the Second Deputy Prime Minister, and other Ministers (see figure 3.3).

Legislative, organisational, administrative and executive powers are vested in the Council of Ministers, to which financial matters, as well as all other affairs relating to different ministries and other government institutions, are referred. Domestic policy, as well as all public affairs of the country including economic and financial matters, education and defence are discussed by the Council of Ministers who make recommendations to the King. Such recommendations are usually accepted. However, those which are not accepted may be referred back to the related committees within the Council of Ministers for further study and review, and re-submission in the following meetings.³

³ At present, it is customary for the Council of Ministers to meet weekly and discuss recent issues in internal and foreign affairs.

Figure 3.3
Structure of the Government System in Saudi Arabia



Source: Adapted from Al-Amri, 1982, p.16

It should be pointed out that the political system of Saudi Arabia differs from that of most developing countries, particularly in the formative stages, in that it does not have a history of exploitation and subjection

by any Western colonial power. As Al-Amri (1982, p.15) pointed out that:

"Most of the developing nations, in their formative stages, were heavily influenced by one or the other of the European nations. Accordingly they patterned their independent system of government after that nations. ... Saudi Arabia, on the other hand, was never a colony. Its relations with other nations were always on a more remote, more equal basis. And when the political system of Saudi Arabia was being formed, it relied on the values of the nation, predominantly those of Islam, rather than on a foreign model."

In addition to being the most influential Arab country and the leader of the Islamic World, the Kingdom has maintained a respected and influential position in the international community. Saudi Arabia is a founder member of the Congress of Islamic World, the Arab League, the United Nations, the Gulf Cooperation Council, the International Monetary Fund and many other International Organisations. Moreover, Saudi Arabia maintains good and strong relations with the USA, Western Europe and Japan.

3.4 Regulatory Environment

In any country, economic and business affairs need to be governed by certain laws. Such laws are usually enacted by government according to the changing needs of society. In this respect, Saudi Arabia is no exception; a number of laws have been enacted. Some of these laws have been amended, or replaced to provide more suitable regulations for the need of the country. However, others still need further study and revision.

Detailing these laws is beyond the scope of this thesis. However, some of them, such as the Companies Law, the Income Tax and Zakat Law, the Certified Accountants Law, and the Foreign Investment Law, will be reviewed because of their relevance to the present study.

3.4.1 Companies Law

The Companies Law was promulgated by Royal Decree No. M/6 in 1965 and amended by Royal Decree No. M/23 in 1982. The Law consists of fifteen sections with a total of 234 articles. The Law determines the legal framework for companies in Saudi Arabia. For example, article 2 of this Law recognizes the following business entities:

- General partnership
- Limited partnership
- Joint venture
- Joint stock company
- Partnership limited by shares
- Limited liability company
- Variable capital company
- Cooperative company

All the above business enterprises, irrespective of their legal status, are required by Saudi Commercial Law to be registered in the Commercial Register within the Ministry of Commerce. The main features of each of the these entities are briefly discussed below.

(a) General partnership

In this form of entity, two or more persons are engaged in business and all partners are jointly and severally liable for business debts. The entity must bear the name of one or more partners, and must state the essential characteristics and purpose of the partnership,

in conformity with the true facts (Art. 17). There is no minimum capital requirement. The General Partnership is the most common form of business organisation used by Saudi nationals.

(b) Limited partnership

This form of entity consists of two types of partner: at least one active partner, liable for the partnership's debts to the extent of his entire assets, and at least one sleeping partner, liable for the partnership's debts only to the extent of his participation in the corporate capital stock (Art.36). The partnership's name shall consist of the name(s) of one or more active partners, and state the partnership's nature, whereas the names of sleeping partners may not appear in the company's name (Art.37). A sleeping partner may not interfere in such activities as are part of external management, not even by proxy. If he does participate in external activities of management, then he will be liable to the same full extent as a general partner. However, he may participate in the internal management of the partnership within the limits laid down in the articles of incorporation (Art.38).

(c) Joint venture

A joint venture is an association of two or more persons, of which association third parties are not aware. Consequently, a third party has recourse only against the party with whom he had dealings. The joint venture is not a legal body and is not subject to the

publication requirements that apply to other companies (Art. 40). Generally, the rights, obligations, terms and other conditions are set forth in a separate agreement between the joint venturers (Art. 43). This is the business format most widely used by foreign joint venturers.

(d) Joint stock company

A joint stock company may be incorporated only by issue of a Royal Decree, which must be requested from the Ministry of Commerce by at least five shareholders. The application must contain the usual information relating to corporations, such as objectives, life span, capital, names of shareholders, and proposed bylaws.

A joint stock company is considered as the biggest business organisation in Saudi Arabia in terms of capital and activities; hence it will be discussed in more detail in chapter 6.

(e) Partnership Limited by Shares

A Partnership Limited by Shares is an association of two different parties; one party consisting of not less than one active partner liable for the partnership's debts to the full extent of his assets, and a second party consisting of not less than four shareholders liable for the partnership's debts only to the extent of their contribution in the corporate capital stock (Art. 149). The total capital cannot be less than SR 1,000,000,⁴ of which at least half must be paid in on formation. The

⁴ This figure was formerly SR 100,000. Current exchange rate is \$=SR 3.75.

capital is divided into equal negotiable shares, each of which must have a minimum par value of SR 50 (Art. 150).

(f) Limited Liability Company

This kind of company is formed by a common act of at least two, but not more than fifty, partners liable for the company's debt, each to the extent of his contribution in the company's capital stock (Art.157). The minimum capital is SR 500,000⁵ and the total capital must be divided into equal non-negotiable shares. The public may not be invited to subscribe for such shares or any increase in share capital (Art.158). The Companies Law prohibits this type of enterprise from undertaking certain activities such as insurance, savings-banks or banking institutions (Art. 159).

(g) Variable Capital Company

This association of two or more partners resembles a limited liability company, except that its memorandum of association or bylaws may permit annual increments of capital, which may come from either existing partners or the admission of new partners.

(h) Cooperative Company

Joint Stock Companies and Limited Liability Companies may be incorporated to carry out a specific cooperative purpose, such as to reduce the cost or selling price of a product or service, to improve its quality, or both. A Cooperative Company shall be subject, as applicable, to the provisions prescribed for Joint

⁵ This figure was formerly SR 50,000.

Stock Companies or Limited Liability Companies (Art. 190). Its instrument of incorporation or its by-laws may provide that the partners shall incur additional liability up to double the amount deriving from their shares, if the company is declared bankrupt or insolvent (Art. 192).

The remaining articles of the Companies Law deal extensively with the basic details of formation, such as registration procedures, minimum capital required, number of partners, number of directors, conversion and amalgamation, dissolution and other related matters. It must be mentioned, however, that the Companies Law includes some accounting guidelines, particularly in the following areas:

i) Companies' Accounts

Companies' Accounts are dealt with in Articles 123-128. For instance, Article 123 requires the Board of Directors to prepare at the end of each financial year an annual statement comprising a survey of the company's assets and liabilities to date, a balance sheet and profit and loss account and report outlining the company's affairs and its financial position during the last year. All these documents shall be made available to the auditor at least fifty five days before the date set for the general meeting of shareholders. Article 124 emphasises consistency in classifying the balance sheet and profit and loss account, and principles used in valuing the assets and liabilities.

ii) Appointment of auditor(s); his independence, rights, duties, and responsibilities

Every company is required to appoint an auditor(s), who must be licensed to practise accounting in the Kingdom of Saudi Arabia. He will be appointed at the General Meeting which also determines his term, fees, and term of office (Art.130). The Law emphasizes the independence of the auditor. In this respect, para 2 of the same Article stipulates that:

"the auditor's mandate shall be incompatible with simultaneous participation in the company's incorporation, with holding the office of director or with being involved with the company in any technical or administrative, albeit advisory, capacity; nor is it permitted for any auditor to be employed by or to be in any way, up to the fourth degree inclusive, related to a partner of any of the company's promoters or directors."

Article 131 states that the auditor has the right to examine all the company's books, records and other documents, and to request any information deemed necessary in the performance of his examination. If he does not have access to the information needed, then he should report this to the Board of Directors at the General Meeting. Moreover, the Companies Law emphasizes the auditor's right when it states that any manager or director who hampers an auditor in the proper execution of his duties shall be punished by a fine of not less than SR 1,000 nor more than SR 5,000 (Art.230 para.d).

With regard to an auditor's duty, Article 132 requires the auditor to give in his report all details and explanations required, and to state any violations of the company's rules and regulations, and his opinion of

the extent to which the company's financial papers are in accordance with the true facts.

Finally, in respect of the legal responsibility of the auditor, Article 133 para 1 states that:

"the auditor shall not, otherwise than at the General Meeting, disclose what he should learn or be told about the company's affairs, in performing his duties; any auditor's failure to observe said provision shall entail his discharge and shall render him liable for damages."

These are the main articles in the Companies Law which deal directly with accounting matters.

3.4.2 The Income Tax and Zakat Law

The Income Tax Law was introduced in the Kingdom of Saudi Arabia for the first time by Royal Decree No 17/2/28/3321 dated 21/1/1370H (1950). Several decrees were issued after that to amend certain rules. One of these was Royal Decree No. M/37 dated 4/5/1395H (1975), which abolished the individual income tax on salaries, bonuses and the like.⁶

At the outset, the law imposed income tax on Saudis as well as non-Saudis. Later, Saudi citizens objected to the imposition of income tax on them due to the fact that at the same time they pay Zakat to needy people. In this respect Shinawi (1970, p.146) states:

"It was argued that Saudis pay Zakat to the poor, a tax governed by religion, and imposing secular income tax on them simply meant tax duplication."

⁶ Recently, a proposal to reintroduce income tax on foreigners was announced in the Official Gazette on January 3rd, 1988. However, the resulting outcry led the government to cancel the plan just two days later (5/1/1988).

However, this problem was solved by Royal Decree number 8634 in 1951 which established what is called "a bi-tax" system whereby Saudis pay Zakat only and non-Saudis pay tax (Ibid).

The income tax law provides the authority for taxation of the income of real persons. It stipulates which persons are taxable, the types of taxable income, tax rates and the amounts of exempt income which are allowed to various classes of taxpayers or certain types of profits. These issues are briefly discussed below.

i) Taxable Income

According to Royal Decree No. 17/2/28/576 of 14/3/1976 (1956), those company profits subject to corporation tax are (Art.10):

- (1) the net profits realised by any non-Saudi company operating in Saudi Arabia or operating both inside and outside Saudi Arabia at any time;
- (2) the earnings applicable to non-Saudi shareholders in the net profits of Saudi companies;
- (3) the earnings applicable to non-Saudi sleeping partners in partnerships;

Non-Saudi individuals are subject to tax on income from capital investment, which is defined as all net proceeds or profits obtained from:

- any business in which the taxpayer has invested movable or immovable capital;
- buying and selling goods of all kinds and descriptions;
- products from land;
- exchange of money;
- hiring or letting of any movable or immovable property including animals, transport vehicles, ships, and other means of transport, and of machinery and equipment.

ii) Tax Rates

Tax rates are varied according to the type of taxpayer, whether individual or company, and income concerned. As mentioned earlier, there is no tax on salaries, wages and related benefits of individuals in Saudi Arabia. However, investment income from professional activities, and shares of partnership income are subject to tax. Tax rates on this type of income range from 5 to 30 percent on income over SR 66,000, while the companies' income tax rates range from 25 to 45 percent on income in excess of SR 1,000,000 (see table 3.2).

Table 3.2
Individuals' and Companies' Income Tax Rates

Category	Annual income in (SR)		Tax Rate
<u>A. Individuals</u>	<u>Over</u>	<u>But not over</u>	
	0	6,000	0
	6,000	16,000	5%
	16,000	36,000	10%
	36,000	66,000	20%
	66,000		30%
<u>B. Companies</u>	<u>Over</u>	<u>But not over</u>	
	0	100,000	25%
	100,000	500,000	35%
	500,000	1,000,000	40%
	1,000,000		45%

Source: Based on the General Director of DZIT letter to the researcher, No. 5827/1 dated 3/6/1410H (1990).

iii) Tax Year

The Tax Law does not designate a particular period as the tax year. A taxpayer may adopt the fiscal year of his choice, provided approval has been obtained and accurate books and accounts are maintained.

iv) Amounts and Expenses Deductible

Initially, all expenses incurred by the business, provided they are necessary and reasonable, are deductible, including (Art.14):

- a. All the ordinary and necessary expenses which the business or enterprise requires and the expenditure of which takes place during the year, including a reasonable amount for the salaries of employees and for any compensations granted for any personal services.
- b. Travel expenses related to the business or enterprise.
- c. Rentals for properties rented in connection with business or enterprise.
- d. Any losses incurred by the business or the enterprise and not compensated for in any way.
- e. A reasonable amount for the depreciation of properties which are used or employed in the business.

The depreciation referred to in (e) above is computed on a straight-line basis. The depreciation rates approved by the Department of Zakat and Income Tax (DZIT) are shown in the following table.

Table 3.3
Depreciation Rates as Authorised by DZIT

Type of Assets	Rate*
- Building	3%
- General turbines	5%
- Drilling and welding equipment	7.5%
- Furniture and Fixtures, electrical equipment, and woodcutting equipment	10%
- Computers and construction equipment	12.5%
- Office equipment	15%
- Compressors, tents, small tools, and coolers	20%
- Automobiles and air conditioners	25%

* Higher rates for depreciation may be used subject to the prior written approval of the DZIT.

Source: Department of Zakat and Income Tax, Riyadh.

v) Exemption

Foreign companies investing capital in an approved economic development in the Kingdom are granted 10 years tax exemption for agricultural or industrial projects, and 5 years tax exemption otherwise, with the exception of companies concerned with petroleum and minerals. This exemption is conditional upon at least 25% of the capital for the project being Saudi (Foreign Capital Investment Law 1979). In addition, special provisions apply to the taxation of air and sea transport, as well as other concessions. For example, petroleum concessionaires are taxed under individual arrangements and the resulting net profits are subject to a special 85% income tax rate (Platt, 1982, p.162).

The Zakat

The Zakat is a religious tax, charged in accordance with Islamic law, on Saudi individuals, wholly Saudi-owned companies, and the Saudi share of profits of companies owned jointly with foreigners. For this purpose, Bahraini, Kuwaiti and Qatari subjects are treated as Saudis.

The Zakat is levied on capital and earnings therefrom; all proceeds, profits and gains from business, industry or personal work; and property or monetary acquisitions of whatever kind or description, including commercial and financial transactions and dividends, livestock, and crops. However, assets not held for resale are exempt. Those subject to the Zakat, who are engaged

in industrial or commercial activities, are required to keep proper accounting records from which their liability may be assessed. Others are assessed on an estimated basis. The rate of the Zakat is 2.5 percent on income and property. Half this is paid to ZITD, and the other half is distributed to the poor by the Zakat-payer.

A joint venture between a foreign company and a Saudi resident is usually required to submit proof to ZITD that the Saudi has satisfied his Zakat obligation with respect to his interest in the venture before the venture receives a tax clearance certificate.

The Income Tax and Zakat Law also includes some accounting and auditing guidelines. For example, the Law requires all companies operating in Saudi Arabia to maintain their accounting books and records in the Arabic language. These books are the general journal, the ledger, and the inventory book. All transactions and commercial dealings are to be submitted in Arabic. Books which are not prepared according to the department's requirements are disregarded, and the tax assessment would therefore be calculated on an arbitrary basis.

In order to determine the income subject to tax, the Department of Zakat and Income Tax accepts financial statements prepared according to internationally recognized practices. However, the DZIT does not specify the international approach to be adopted. Merei (1985, p.43) pointed out that:

"Since the Tax Authority has not yet defined the term "internationally accepted", any

support for an accounting treatment is accepted. Some firms in Saudi Arabia make reference to the standards issued by the International Accounting Standards Committee; others are using the US Generally Accepted Accounting Principles (GAAP); a few are using Canadian standards ; possibly others use the British GAAP."

With regard to the assessment of the Zakat, the Law requires all individuals and companies engaged in commercial or investment activities to maintain organised accounting records showing the capital and the proceeds and expenses relating to the enterprise during the year so that they can be relied on for the assessment of Zakat. The Law emphasizes the accuracy of such books when it states that "these books and records should be certified by commercial court or public Notary..." (Art.6).

Article 9 requires the Zakat's Officer to check the information submitted by individuals and companies, and he shall reserve the right to check the books and records of the Zakat-payer, when necessary. When satisfied, he shall inform the Zakat-payer of the amount he should pay by sending him an official notice.

3.4.3 The Certified Accountants Law

The Certified Accountants Law was enacted by Royal Decree No. 43 in 1974. This Law, which is still in effect, was the first to regulate the accounting profession in Saudi Arabia. The Law contains thirty-five articles, which deal with the basic requirements of practising accounting services such as qualifications, registration procedures and fees, responsibility of the auditor, violation and trial proceedings, and other

related issues. Since the provisions of this Law are entirely related to the accounting profession, it will be discussed in detail in chapter five, "Accounting Profession in Saudi Arabia".

3.4.4 The Foreign Investment Law

The Foreign Capital Investment Law was enacted by Royal Decree No. M/4 in 1979, and applies to all capital owned by a non-Saudi individual or by a corporation which has non-Saudi shareholders. Capital is defined to include cash, securities, fixed assets, raw materials, products, spare parts and patents and trademarks.

Prior to commencement, all projects involving foreign capital must obtain an industrial licence, issued by the Ministry of Industry and Electricity on the recommendation of its Foreign Capital Investment Committee (FCIC). The necessary qualifications are that the investment should be in projects which further the economic development of the economy. These are taken to include maintenance, health and contracting as well as industrial projects, and those where there will be a transfer of foreign technology and expertise. Separate licensing procedures relate to petroleum and mineral extraction projects.

According to this Law, investors should first apply to the Foreign Investment Bureau (FCIB) at the Ministry of Industry and Electricity. The application is first studied by the Department of Industrial Licences and, if it is accepted, the investor should prepare a feasibility

study within six months. A direct application for an industrial licence can be made if the feasibility study has already been prepared.

The application to the FCIB for an industrial licence should be in triplicate, in Arabic with an English translation, and should be accompanied by:

1. The feasibility study;
2. Details of the foreign investor's previous project experience both within and outside Saudi Arabia;
3. A copy of the approval of the Board of Directors or owners of the foreign firm for the project;
4. A copy of the agreement between the foreign and Saudi investors;
5. A copy of the home registration certificate of the foreign company; and
6. Copies of machinery catalogues and quotations relating to the project.

The application is then evaluated by the FCIB which reports to the FCIC. This committee in turn makes a recommendation to the Minister of Industry and Electricity on acceptance or rejection. If accepted and approved by the Minister the committee will then issue an industrial licence.

3.5 Economic Environment

The economic environment in Saudi Arabia may be divided into three periodic phases: (a) the period before the discovery of oil in 1938; (b) the period between the discovery of oil and 1970 when the First Five-year Development Plan was introduced; and the planning phase (1970 to the present).

3.5.1 Before the Discovery of Oil

At the time of its establishment, the Kingdom of Saudi Arabia had no oil revenues. The main source of revenue was pilgrimage, which yielded an insignificant sum of not more than a million pounds sterling per year. To make matters worse, the founding of the Kingdom coincided with the period of the great depression, during which the number of pilgrimages - and consequently revenues - had been fast declining. Although there were some other activities such as fishing, pearling, agriculture, ship-building, and commerce, no adequate statistics exist to show the relative importance and volume of each of these activities.

In summary, before the discovery of oil, socio-economic environment was such as to classify Saudi Arabia as a poor or traditional country. Most of the population were nomadic, or living in small towns and villages. The overall economy was based upon revenues received from pilgrims to the holy cities of Mecca and Medina and some income from grazing and agriculture.

3.5.2 After the Discovery of Oil

Oil was first discovered in 1938, and it was only after World War II that production increased rapidly. As a result of the rise in oil output and revenues, the first formal national budget was prepared in 1948. However, during the 1950s, oil revenues were affected by fluctuations in the world oil market.

By 1960, oil production began to increase rapidly again. As a result, the Kingdom's economy recorded a high rate of growth. According to Knauerhase (1975, p.84), this rate of growth represents a remarkable achievement rivalled only by the growth rates of Japan and West Germany during the 1960s.

While progress during the 1960s was indeed spectacular, the Middle East crisis of 1967, brought to the fore inherent weaknesses in the Saudi economy. Apart from its heavy dependence on oil, the economy had become increasingly reliant on imports for both consumer goods and capital equipment. The closure of the Suez Canal and intermittent disruptions of the Tapline, due to the Arab-Israeli war, adversely affected the Kingdom's oil exports as well as essential imports. As a result of all these events the balance of payments went into deficit for the first time in nine years. To maintain the economy and to restore its former pace of development, efforts to introduce a comprehensive five-year development plan were begun in 1970. This marked the beginning of a new era of the Saudi Arabian economic environment.

3.5.3 The Development Planning Phase

This phase started in 1970 when the Government launched the first comprehensive development plan for a five year period. So far, four development plans have been implemented and now the fifth plan is half way to completion (see table 3.4).

Development planning in Saudi Arabia is based on two basic principles: the maintenance of religious values and the provision of national security. Beyond these fundamental principles, several other broad goals have guided the first four plans, and will continue to provide the framework for future plans (Fifth Development Plan, 1990-95, p.4):

- Diversifying the economy and reducing dependence on oil;
- Raising living standards and improving the quality of life;
- Maintaining economic and social stability
- Regional Development;
- Strengthening the role of the private sector in the economy;
- Broadening the linkages between the Kingdom and other nations;
- Developing and completing the physical infrastructure;
- Developing human resources.

Table 3.4
Development Plan Durations

Development Plan	Duration
First Development Plan	1970 to 1975
Second Development Plan	1975 to 1980
Third Development Plan	1980 to 1985
Fourth Development Plan	1985 to 1990
Fifth Development Plan	1990 to 1995

Within the broad context of these long term goals, each plan has had its own particular focus, reflecting

both the stage of development in the Kingdom at the time and the resources available to the government. The main features of each of these plans are outlined below, with greater emphasis upon the fifth plan, as it is closer to the present study.

3.5.3.1 The Main Features of the First Development Plan (1970-75)

The first plan covered the period from 1970 to 1975 and was the first comprehensive approach to economic development in Saudi Arabia. The plan was launched under stringent financial difficulties, one of which was the deficit in the balance of payments in the two preceding years. It has been described as modest in size, about SR 80 billion, spent mainly on developing the basic infrastructure, particularly public utilities, and on improving government services (Fourth Plan, 1995-90, p.4).

3.5.3.2 The Main Features of the Second Development Plan (1975-80)

The formulation of the second plan was unconstrained by finance. However, inflation was the major problem facing the Kingdom during the implementation of the plan.

"It was during the second plan that the Kingdom faced one of its major challenges, as inflation rose to very high levels mid-way through the implementation of the plan" (Ibid).

This inflation was attributed to the increase in oil price from October 1973 which had resulted in a rapid increase in revenues and the fact that development was

proceeding at a far greater pace than had been anticipated in the first plan.

The second plan gave priority to agricultural and industrial expansion as avenues for diversification of the economy. There was continued emphasis on the development of physical infrastructure to avoid bottlenecks in the anticipated growth of productive sectors. Several incentives, such as credit facilities and subsidies, were proposed to encourage private enterprise in both agriculture and industry.

3.5.3.3 The Main Features of the Third Development Plan (1980-85)

The third plan was formulated with three fundamental objectives (Third Plan, 1980-85, p.37):

1. to promote structural change in the economy through emphasis on resource development and growth in production sectors;
2. to increase economic and administrative efficiency;
3. to increase participation in the development process, thereby raising the overall level of social welfare.

The authors of the third plan pointed out that it was no longer necessary to give first priority to infrastructure development. Accordingly, the plan shifted the emphasis to the development of the productive sector. It pressed for the completion of ongoing infrastructure projects, while emphasising the need for more output-oriented investment by the public sector, as well as more output from the production sectors, and for continuing development of manpower. Another government policy during

the third plan was to reduce the level of foreign manpower which had increased during the previous plan.

3.5.3.4 The Main Features of the Fourth Development Plan (1985-90)

The fourth plan was formulated with the following main objectives (Fifth Plan, 1990-95, p.17):

1. to continue structural change in the economy through diversifying the economic base and reducing dependence on crude oil as the main source of national income;
2. to encourage the rapid development of the private sector as the principal mechanism for achieving economic diversification;
3. to improve the economic efficiency of the government sector;
4. to complete the infrastructure projects necessary to achieve long term economic and social development;
5. to develop further the Kingdom's human resources.

The government allocated SR 1,000 billion to achieve the above objectives. However, the weakening world oil markets in the early years of the fourth plan caused government revenues to fall below their anticipated levels. Accordingly, expenditures were reduced by 20 percent below the planned level. This shortfall in government expenditure, coupled with the private sector's uncertainty over the economic outlook, prevented the plan's growth targets from being achieved (Ibid. p.17-18).

3.5.3.5 The Main Features of the Fifth Development Plan (1990-95)

The Fifth Plan came into effect on January 1990. The following are the main objectives of the plan, as established by the Council of Ministers (Fifth Plan, 1990-95, p.45):

1. To safeguard Islamic values by duly observing, disseminating, and confirming Allah's Sharia (God's Divine Law);
2. To defend the Faith and the Nation, and to uphold the security and social stability of the Kingdom;
3. To form a productive national work force by encouraging citizens to avail themselves of the benefits from the infrastructure and institutions provided for them by the State - ensuring their livelihood and rewarding them on the basis of their work;
4. To develop human resources, thus ensuring a constant supply of manpower, upgrading its quality and improving its efficiency to meet the requirements of the national economy;
5. To raise cultural and information standards to keep pace with the Kingdom's development;
6. To reduce dependence on the production and export of crude oil as the main source of national income;
7. To continue with real structural changes in the Kingdom's economy so as to establish a diversified economic base - with due emphasis on industry and agriculture;
8. To develop mineral resources and to encourage discovery and utilization thereof;
9. To concentrate on qualitative development of already established utilities and facilities by improving their level of performance;
10. To complete the infrastructure projects necessary to achieve overall development;
11. To further encourage private sector participation in socioeconomic development;
12. To achieve balanced growth throughout all regions of the Kingdom;

13. To achieve economic and social integration among the Gulf Cooperation Council (GCC) countries.

The Government allocated SR 753 billion for expenditure on the fifth plan. This figure includes civilian and non-civilian items distributed as shown in table 3.5.

Table 3.5
Planned Government Expenditure in the Fifth Plan
(SR million)

Expenditure	amount	%
Total expenditure,	753,000	100
of which:		
civilian	498,000	66
non-civilian	255,000	34
Civilian expenditure:		
Development agencies,	395,000	79
of which:		
human resources	140,000	
economic resources	73,000	
infrastructure	116,000	
social and health	66,000	
Other	103,000	21

Source: Compiled from the Fifth Development Plan (1990-95), Ministry of Planning, Riyadh, Saudi Arabia.

The Fifth Development Plan, with its objectives and methodology, is considered to be a continuation of the previous plans, and an extension of their long-term objectives. The fifth plan has placed more emphasis on the following aspects:

- Expansion of the government revenue base with the aim of increasing non-oil revenues.

- Ensuring and maintaining stability of the national economy through the adoption of a stable methodology for annual government expenditures.

- Consolidation of reliance of the national economy on the activities and available resources of the private sector, by stimulating national capital for investment within the Kingdom.

- Providing job opportunities for the Saudi work force.

- Substitution of local imports for foreign imports, and effective penetration in the export markets by consolidating the competitiveness of national industries, and hence increasing the volume of exports and improving the position of the balance of payments.

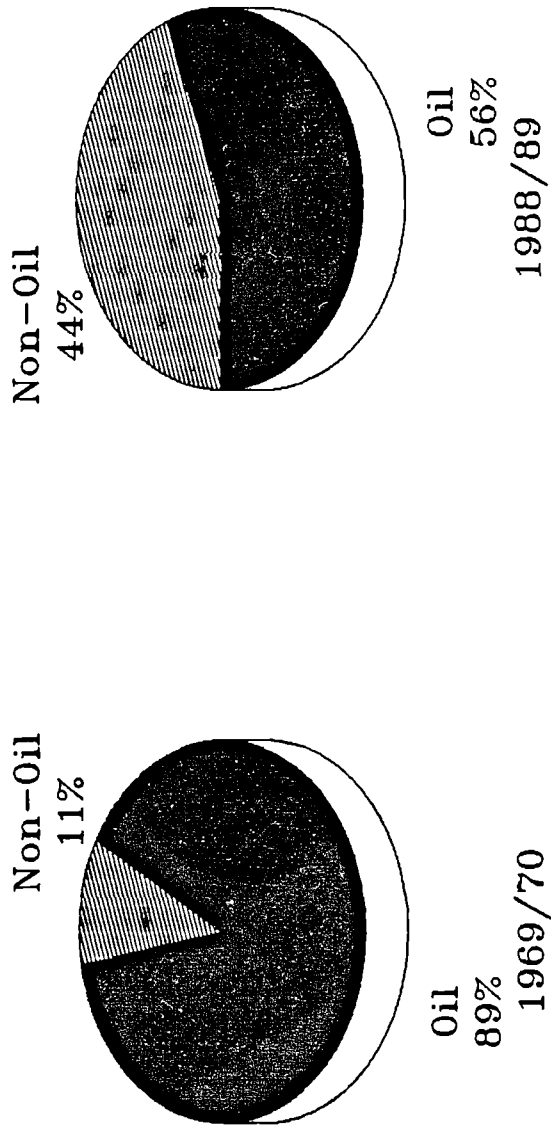
- Expansion and diversification of the economic base by means of exerting continuous efforts to increase the contribution of production sectors toward the national economy, along with the adoption of new initiatives which will pave the way for the private sector to carry out its activities effectively.

- Placing more emphasis on the realization of balanced development in the Kingdom's various regions.

3.5.4 Achievements of Development Plans

According to the Ministry of Planning, the Kingdom of Saudi Arabia has achieved far more in twenty years of development planning than many other nations have accomplished in as many decades. Great progress has been made in each major area of development. The Ministry of Planning has issued a lengthy document showing what was achieved during the first four plans; this document will be used extensively in this section.

Figure 3.4 Percent Distribution
of Government Revenues



Source: Ministry of Planning,
Achievements of the Development Plans,
1970 - 1989

As stated earlier, one of the main objectives in all previous development plans was to diversify the economy and reduce dependence on oil. In 1969/70 the government received 89% of its revenues from oil while only 11% came from non-oil revenue, whereas in 1988/89 oil revenue accounted for 56% while non-oil revenue accounted for 44% as shown in figure 3.4.

With regard to raising living standards and improving the quality of life: during the past 20 years national income has increased more than fourfold in real terms, reaching a value of SR 280 billion in 1989; personal consumption has increased at an average annual rate of 9.4 percent in volume terms; infant mortality has dropped from 148 per 1000 live births in 1970 to about 43 in 1989; and the number of physicians in the Kingdom has grown from 1200 in 1970 to more than 20,000 in 1989, while the number of hospital beds has increased from 11,000 to over 38,000.

With regard to strengthening the role of the private sector: the real output of the private sector has grown fivefold in volume during the past 20 years; private investment has increased sevenfold in real terms; employment in the private sector has increased by 3.9 million; and the number of registered corporations has risen from less than 1000 in 1970 to over 7000 in 1989.

With regard to developing physical infrastructure: during the past two decades the paved road network expanded from about 8000 kilometres in length to more

than 32,000 kilometres; the number of working telephone lines rose from 29,000 twenty years ago to 1,500,000 in 1989; installed electricity generating capacity increased from 418 megawatts in 1970 to 14,570 megawatts in 1989; and desalination plants increased their water output from less than 20,000 cubic metres per day in 1970 to almost 1,500,000 cubic metres per day in 1989.

With regard to developing human resources: over the past 20 years, school enrolments have increased by 192 percent at the elementary level, 375 percent at the intermediate level, and 712 percent at the secondary level, while vocational training has increased by 1575 percent; the total pupil and student population increased from around 600,000 in 1970 to 2,500,000 in 1989; and seven universities and eleven girls colleges have been established, with a current enrollment of more than 120,000 students. The annual number of university graduates has grown from 1,100 in 1970 to 13,000 in 1989.

3.5.5 Local Capital Market

Up to now there are no formal capital or money markets in Saudi Arabia. However, the principal responsibility for mobilising and distributing private capital among sectors rests with the commercial banks, which are regulated by the Saudi Arabian Monetary Agency (SAMA) which also functions as a central bank. The regulations cover a range of aspects of operation, from branch expansion to operating hours and authorised charges for services. All commercial banks in Saudi

Arabia are required to submit financial and statistical returns to SAMA on regular basis. SAMA also requires all banks to submit annual audited financial statements.

The policies adopted since 1976 have tended towards Saudisation, so that the Saudi side would hold at least sixty percent of the capital of each bank. This process has been effected on a gradual basis, and by 1982 all branches of foreign banks had been converted into joint venture banks. The Saudisation process led to several important results, including the increasing number of branches operating in Saudi Arabia, from 79 in 1975 (the year prior to the Saudisation process) to 1010 branches in 1989.

As at the end of financial year 1989, there were twelve commercial banks in Saudi Arabia, of which three were wholly Saudi and the other nine all had a foreign holding. The three wholly Saudi banks are Riyadh Bank, a joint stock bank 47% owned by government; National Commercial Bank, the Middle East's largest privately owned bank; and Al-Rajhi Banking Investment Corporation, a public shareholding bank. Table 3.6 shows a list of the 12 commercial banks in Saudi Arabia, their paid up capital (in millions Saudi Riyals) and the number of branches each bank had in the Kingdom as at the end of 1989.

Table 3.6
Commercial Banks in Saudi Arabia

Name of Bank	Paid Capital		No. of Branches
	Values	%	
1. National Commercial Bank	N/A	000	226
2. Riyadh Bank	200	5,0	159
3. Saudi Cairo Bank	100	2,6	47
4. Saudi French Bank	90	2,3	62
5. The Arab National Bank	210	5,4	108
6. Saudi British Bank	400	10,3	40
7. Bank Al-Jazira	400	10,3	26
8. Saudi American Bank	600	15,4	35
9. United Saudi Commercial Bank	300	7,7	12
10. Saudi Duch Bank	600	15,4	28
11. Saudi Investment Bank	250	6,4	7
12. Al-Rajhi Bank	750	19,2	260
Total	3900	100	1010*

* Excluding 38 seasonal Branches

Source: Compiled from Saudi Corporations (Council of Saudi Chambers of Commerce and Industry, Riyadh, December 1989); and SAMA Statistical Summary 1990.

Apart from the 12 commercial banks there were six government Specialised Credit Institutions (SCIs), which provide medium- to long-term interest-free loans, with a low handling charge of about 3%. They are not regarded as competitors to the commercial banks, which deal in short term loans. The total loans distributed by SCIs since their inception have exceeded SR 234 billion by the end of 1989, and they are expected to provide nearly SR 37 billion in loans during the Fifth Development Plan (1990-95).

Share trading was not popular among the general public in Saudi Arabia until very recently. Prior to 1985, share trading in Saudi Arabia was very limited, and even when it took place was carried out through small

broker offices with non-professional staff. Such offices were found in the major cities throughout the country and operated under trade commission licences, which did not chiefly cover share trading activity. This system suffered from many shortcomings. Among these, were high variations in share prices from one broker to another, long delay in transferring share ownership and sometimes share certificates could be bought and sold several times before reaching the last buyer.

Table 3.7
Shares Traded Through Commercial Banks as in 1988/89

Shares Listed (SR billion)	80.6
Shares Traded (SR billion)	1.9
Value Traded as Percent of Listed Value	2%
Number of Shares Traded (million)	14.6

Source: The Fifth Development Plan (1990-95), Ministry of Planning, Riyadh, Saudi Arabia, p.164

In 1985, the SAMA took share trading out of brokers' competence and handed it over to the above 12 banks, giving them exclusive control over trading. The banks were not allowed, however, to act as market makers. Their role was virtually limited to matching buy and sell orders for clients. In the absence of a computerized trading network, dissemination of information remained quite unsatisfactory. These and other shortcomings of the current exchange mechanism have been emphasised recently by the Fifth Plan (1990-95, p.164) in the following statement:

"The current stock exchange mechanism is rather slow and very complicated, as the processing of a stock issue can take up to two years. Individual stock transactions require between one week and two months to complete and, more often than not, the buyer must reach the seller by his own means. Thus, blocks of shares may not be broken up to match the needs of buyers. These obstacles result in significant gaps between bid and asking prices, thus indicating that the price mechanism is not working efficiently."

In order to overcome these shortcomings, the Fifth Plan calls for the establishment of a more effective stock exchange. However, the government is still cautious about this matter; it believes that it is too early for such a decision, as the tradeable share volume is still too small (see table 3.7) and the public understanding of share investment is confined to speculation only.

3.5.6 Foreign Trade and Balance of Payments

The Saudi Arabian economy is foreign trade oriented owing to its high dependence on imports and the large quantity of crude oil it exports. The significance of foreign trade to the national economy comes from the unique position of Saudi Arabia in the world economy, which is characterised by the following (the Fifth Development Plan 1990-95, p. 108):

1. The Kingdom is the world's leading crude oil exporter.
2. The Kingdom holds substantial public financial assets abroad in the form of liquid reserves and other investments. The private sector also has its own foreign investments.

3. The Kingdom has emerged on the international scene as an exporter of processed goods, and in particular, petrochemicals.

Table 3.8 shows Saudi Arabia's exports, imports and the trade balance. Saudi Arabia's exports consist mainly of oil and refined products. Its imports are represented by machines, transport equipments, foodstuffs and clothing and textiles.

Table 3.8
Total Value of Exports, Imports and the Balance of Trade
(1973-1989 in Millions SR)

Year	Exports	Imports	Trade Balance
1973	33,309	7,310	25,999
1974	126,223	10,149	116,074
1975	104,412	14,823	89,589
1976	135,154	30,691	104,463
1977	153,209	51,662	101,547
1978	138,242	69,180	69,062
1979	213,183	82,223	130,960
1980	362,886	100,350	262,536
1981	405,481	119,298	286,183
1982	271,090	139,335	131,755
1983	158,444	135,417	23,027
1984	132,299	118,737	13,563
1985	99,536	85,564	13,972
1986	74,378	70,781	3,597
1987	86,880	75,313	11,567
1988	91,288	81,582	9,706
1989	106,241	79,219	27,022

Source: Computed by the author from SAMA Statistical Summary, 1990

It is clear from the above table that Saudi Arabia enjoyed a substantial trade surplus even before the oil price rises of 1974. This surplus grew substantially after 1974 and again in 1979 with further oil price rises.

The overall balance of payments situation, however, is less favourable than the balance of trade. The current account of the balance of payment was affected by the

performance of the trade balance in recent years. Table 3.9 shows the current account deficit in the second half of the 1980s.

Table 3.9
Balance of Payments (1985-1989)
(\$ million)

	1985	1986	1987	1988	1989
Exports	27,393	20,025	32,138	22,964	28,500
Imports	-20,364	-16,620	-17,797	-19,220	-21,000
Balance	7,029	3,405	14,341	3,744	7,500
Services					
Exports	16,065	13,944	13,303	13,364	13,507
Imports	-27,578	-21,440	-19,506	-19,993	21,210
Balance	-11,513	-7,496	-6,203	-6,629	-7,703
Transfers (net)					
Private	-5,199	-4,804	-4,935	-4,900	-4,802
Official	-3,249	-3,000	-3,300	-2,500	-2,500
Total	-8,448	-7,804	-8,235	-7,400	-7,302
Current Account					
Balance	-12,932	-11,895	-9,583	-10,285	-7,505

Source: Compiled from MEED Profile 5, Saudi Arabia Towards an Industrial Society, March 1990, p.37.

According to the Ministry of Planning, these deficits are the results of two forces. Firstly, the deterioration in the World oil market which has adversely affected export revenues from oil, and secondly, the Kingdom's commitment to safeguard the living standards of its citizens and continuation of its development programmes (Achievements of the Development Plans, 1987, P.32)

3.5.7 The Role of the Private Sector in the National Economy During the Fifth Plan

It has been determined that the private sector "encompasses of all economic activity which is not

performed by the government or government-owned companies." (Fifth Plan, p.135).

Development objectives and strategies have emphasised the need to enhance the private sector so that it can play a more effective role in the national economy, by taking part in the process of developing the production, industrial, agricultural and minerals sectors. This is a policy that aims at intensified structural changes in the national economy. The Fifth plan also includes several measures that aim to support the private sector and consolidate its participation in the promotion of the various development sectors, as it is considered to be the cornerstone for realization of overall socio-economic development. Thus, emphasis will mainly be placed, during the coming years, on developing policies necessary for encouraging the private sector to assume its role, realizing close cooperation between the public and private sectors in order to provide the private sector with opportunities for the establishment of new private organisations, which will provide services of a high standard, commensurate with the quality of services previously undertaken by the government.

The role of the private sector and the investment of its resources within the Kingdom are considered to be among the key issues during and beyond the fifth plan period. It is imperative to pave the way for investment in this sector, so that it can effectively make use of the available opportunities in the national economy and

in the international exports markets. Consequently, the fifth plan places more emphasis on ensuring a healthy atmosphere for consolidating and increasing economic activities through providing government policies, regulations, financial incentives and data necessary for the encouragement of these activities. It is hoped by these means to realize the fifth plan objectives which call for boosting the dependence of the national economy on the activities and resources of the private sector by stimulating national capital for investment within the Kingdom. Regulations and rules will also be introduced to finance some development programmes and projects through private firms and establishments under government supervision and guarantee.

Furthermore, an important institutional measure concerning the development of the private sector is the establishment of a private sector department within the Ministry of Planning. The main function of this department will be to ensure the coordinated development and implementation of policies affecting the investment climate and operations of the private sector in the Kingdom (Fifth Plan, p.145).

3.6 Summary and Conclusion

The main purpose of this chapter has been to explain the basic environmental background in which accounting operates in Saudi Arabia. The emphasis was upon Saudi Arabia's social, political, regulatory, and economic environment. It was shown that Saudi Arabia is an Islamic

State in which religion plays an important role in the political, social and economic affairs of the Kingdom.

It was also shown that unlike most developing countries, Saudi Arabia has never been a colony or subject to foreign rule. Its political system is based on the Holy Qura'n and traditional Sharia (Islamic Law) and all decisions of the government are guided by them. In spite of all the changes and developments in Saudi Arabia, Islam has remained at the centre of all the activities and has been the ultimate guiding force.

The Government of Saudi Arabia, by means of the Council of Ministers' Resolutions and Royal Decrees, has enacted a numbers of laws which include Companies Law, Income Tax Law, Certified Accountants Law and Foreign Investment Law. Some of these laws have been amended, or replaced, to provide regulations better suited to the needs of the country. However, others still need further study and revision. The positive aspect of these laws is that they include some accounting and auditing guidelines, particularly with regard to the company's accounts, appointment of the auditor; his independence, rights, duties, and responsibilities. However, nothing has been stated about the format, layout, procedures and contents of financial reports in any of these laws.

Although Saudi Arabia was founded as a Kingdom in 1932, much of its economic development took place in the last two decades. It was only in the 1970s that efforts were made to develop the economy, and create a national

infrastructure of modern highways, ports, airports, schools, and hospitals. With the oil price rises in 1973-74 the resources to finance development increased enormously, and there was a rush to create a modern infrastructure as quickly as possible. The speed of implementation resulted in some waste, but overall the first, second and third development plans were successfully implemented, and the structure for a modern unified economy created. However, in recent years the pace of development has slowed, partly reflecting oil production cut-backs and then price falls with a marked deterioration in terms of trade. At the same time, less investment has been needed, with the completion of major infrastructure projects.

The Fifth Plan (1990-95), envisages the private sector playing a more effective role in the economy by helping to develop the production, industrial, agricultural and mineral sectors. The plan indicates that the right atmosphere should be created to stimulate these sectors. This will require management regulations, financial incentives and more information about investment possibilities. It should be pointed out, however, that the development of accounting has not been explicitly included in any of the development plans implemented so far, nor in the current plan.

PART II
STATUS OF ACCOUNTING SYSTEM
IN SAUDI ARABIA

CHAPTER 4

ACCOUNTING EDUCATION IN SAUDI ARABIA

4.1 Introduction

Accounting education undoubtedly plays a significant role in the development of an accounting system, particularly in a developing country, which has witnessed rapid economic change.

"The need for broadly educated accountants is nowhere more important than in the developing countries, such as those in the Arab world, where environments change constantly." (Agami and Alkafaji, 1987, p.161).

Unfortunately, accounting education in Saudi Arabia has received little attention from accounting researchers, both locally and internationally. Locally, for example, the Saudi Accounting Association (SAA) has held four symposia concerning the development of accounting in Saudi Arabia since its establishment in the early 1980s; only one paper presented in the first symposium dealt with the subject of accounting education.¹

The purpose of this chapter, therefore, is to examine the main features of accounting education in Saudi Arabia. However, because accounting education operates within the framework of the education system as a whole, it is necessary to explain the basic features of the general education system of Saudi Arabia.

¹ See Dr. Sultan M. Al-Sultan, "The Role of Universities in the Preparation of Statutory Accountants", Accounting Development Symposium, King Saudi University, Riyadh, 25 March, 1981.

The next section therefore provides brief background information about the education system in Saudi Arabia. It reviews the principles and objectives of education, discusses how the education system is organized and briefly reviews educational financing in Saudi Arabia.

The rest of the chapter (section 3 onwards) is devoted to accounting education in Saudi Arabia. It starts by examining accounting education below university level, which includes the accounting courses offered by secondary commercial schools and Higher Institutes for Financial and Commercial Science. University accounting education is then discussed, with particular reference to the accounting curriculum at both undergraduate and postgraduate level, accounting teachers, teaching methods and techniques. Finally, some problem areas in accounting education in Saudi Arabia are identified and discussed.

Information used in writing this chapter is based on various official documents, catalogues and bulletins, most of which were in Arabic and had to be translated into English by the author. In addition, the author has drawn on his experience as a student in both a secondary commercial school and the accounting department at King Abdul Aziz University where he presently serves as a teaching assistant.

4.2 General Background to the Education System in Saudi Arabia

4.2.1 Historical Perspective

The history of education in Saudi Arabia goes back to the early decades of this century, even before the unification of the "Kingdom" in 1932. The process of establishing schools instead of "Kuttab" (a method of education mainly taking place in the mosque) is explained by Abd-Al-Wassie (1970, p.4), the former Deputy Minister of Education, as follows:

"In 1903, Hagg Mohammed Ali Zeynel founded a regular Arab school in Jeddah and another in Mecca, known to the present day under the name of the "Falah School". These two pilot schools carried the message of education throughout the years and, in recognition of their efforts, the government has endowed them sufficiently so they can continue and develop their activities. In addition, history records other examples of individuals and collective efforts in education; Dar-Al-Hadith founded by Shaikh Abou-Samh in Mecca in 1932, and the Desert School founded near Medina in 1941 by Ali and Osman Hafez for children of the Bedouin population."

In 1924, King Abdul Aziz established the General Directorate of Education. This Directorate was the nucleus for the present Ministry of Education and its main objectives were to direct and supervise education at all levels.

In 1953, the Ministry of Education was established, and was put into the hands of the Custodian of the Two Holy Mosques, King Fahad Bin Abdulaziz, who was the first Minister of Education in the Kingdom of Saudi Arabia.

Until the mid 1950s, formal education was conducted entirely according to Islamic tradition and it was available to the male population only; education of girls was totally ignored (Kneuerhase, 1975, p.215).

While the teaching of Islam and the maintenance of Islamic Values have remained the focal point of the education system in Saudi Arabia, the attitude towards women's education has changed in recent decades and now women have equal opportunities with men at all educational levels. Indeed, a special government body called the "General Presidency of Girls' Education" was established in 1960 to control and supervise the education of girls at all levels (see sec. 4.2.4).

4.2.2 Principles and Objectives of Education in Saudi Arabia

Education principles in Saudi Arabia stem from Islam. The Educational Policy Document (1974) describes the main principles of education as follows:

- 1) Belief in Allah as the only God, Islam as the Religion and Mohammed as God's Apostle and Messenger.
- 2) Total Islamic concept of life, the Universe and of Man.
- 3) Seeking Knowledge is the obligation of each individual and it is the duty of the State to provide and spread education.
- 4) Recognizing women's right to obtain suitable education on equal footing with men in the light of the Islamic laws.
- 5) Relating education in all stages to the State's general development plan.
- 6) Conscious interaction with international development in cultural fields.

- 7) Using Arabic as the language of instruction at all stages.

Based on the above principles, the Education Policy Document states the objectives of education which also stress Islam and its teachings. Article 28, for example, defines the general objectives of education as:

"... to have the student understand Islam in a correct comprehensive manner, to plant and spread the Islamic creed, to furnish the student with the values, teachings, and ideals of Islam, to equip him with various skills and knowledge, to develop his conduct in constructive directions, to develop the society economically, socially, and culturally, and to prepare the individual to become a useful member in the building of his community."

While the Saudi Arabian government stresses the moral and religious aims of education, its interpretation of Islamic precedent leads it to expect educational institutions to supply the country with faithful Moslem technicians and scientists needed for the development of its human and natural resources.

3.2.3 Structure of the Educational System in Saudi Arabia

3.2.3.1 General Education

General education concentrates on the general, cultural preparation of the younger citizens, built on Islam as a belief, behaviour and an integrated way of life applicable everywhere and at all times (Education Policy, 1974).

General education in Saudi Arabia comprises three stages:

The Elementary stage consists of six grades. Children are expected to enrol in an elementary school at the age of six and leave it at the age of twelve. This stage is designed to equip the children with the elements of Islamic culture and teaches them the basic skills in reading, writing and arithmetic.

The Intermediate stage lasts for three years, during which the students are required to master the basic skills they have acquired in the previous stage. Students are further trained in the proper way of thinking and acquiring practical skills. Moreover, at this stage students start to learn English as a foreign language.

The Secondary stage also consists of a three-year programme. Based on the traditional approach, in the first grade of the programme, students are taught common subjects. Starting from the second grade onwards, students choose either the science or arts section. However, this traditional approach is gradually changing towards a new one based on the credit-hour system. At the end of the third grade of the programme, a public examination is conducted under the supervision of the Ministry of Education. Successful students are awarded a general secondary education certificate which entitles them to join any higher education institution.

Table 4.1 provides statistical information concerning general education in Saudi Arabia. This includes the numbers of students, teachers, and institutions in the three stages (elementary,

intermediate and secondary) as at the end of the 1987/88 academic year.

Table 4.1
General Education in Saudi Arabia key facts, 1987/88*

Category	Male	Female	Total
<u>Number of Students</u>			
Elementary	821,510	663,153	1,484,663
Intermediate	246,004	179,539	425,543
Secondary	104,157	90,538	194,695
Total	1,171,671	933,230	2,104,901
<u>Number of Teachers</u>			
Elementary	50,643	37,671	88,314
Intermediate	17,931	12,477	30,408
Secondary	6,492	6,458	12,950
Total	75,066	56,606	131,672
<u>Number of Institutions</u>			
Elementary	4,668	3,370	8,038
Intermediate	1,548	958	2,506
Secondary	574	416	990
Total	6,790	4,744	11,534

* The Table includes only the schools under the Ministry of Education and the General Presidency of Girls' Education.

Source: The Ministry of Education and the General Presidency of Girls' Education [published in SAMA's Annual Report, 1988, p.118].

4.2.3.2 Technical and Vocational Education

The Government has paid particular attention to the development of technical education in order to prepare the qualified manpower needed for different types of technical duties. Technical education covers industry, commerce and agriculture.

In the commercial field, technical education is divided into two levels, higher and secondary. At the higher level, there are two institutes, one in Riyadh and the other in Jeddah, offering regular full-day and evening classes. At the secondary level, there are eleven secondary schools for commercial education throughout the Kingdom.

In the industrial field, there is the Higher Technical Institute in Riyadh. In addition, three intermediate technical colleges were opened during 1987/88 in Jeddah, Dammam and Qassim. Apart from these institutions, there are eight secondary industrial institutes (SAMA, Annual Report, 1988, p.117). The aim of industrial technical education is to train technicians in the various technical trades such as machine shop, electricity, auto machines, radio and television, and civil engineering.

Finally, in agricultural education, there is the Model Agricultural Institute in Buradah. The Institute prepares technical manpower for the agricultural sector and provides training in plant production, plant protection, animal production, agricultural industries,

horticulture, agricultural mechanization, and other general subjects.

4.2.3.3 Adult Education

Adult education provides for persons who lack adequate schooling and are above the age corresponding to the elementary stage of education. It takes place in adult education centers throughout the Kingdom. The adult education programme consists of two stages: a 16-month preliminary stage to combat illiteracy is succeeded by a follow-up stage of equal duration.

The total number of persons (male and female) enrolled in the adult education programme had reached 146,818 in 1987/88, an increase of 7 percent over the preceding year (Ibid.).

4.2.3.4 Higher Education

The Saudi Arabian Supreme Board defines higher education as follows:

"Higher education is the stage of academic specialization, in all its forms and at all its levels, for competent and gifted students, in order to develop their talents and fulfil the various present and future needs of the society in compliance with useful progress in order to achieve the objectives of the nation and its noble goal."

Higher Education in Saudi Arabia comprises all the stages of formal education following the completion of the different types of the secondary stage courses. This level of education is offered by the universities and by the colleges of Girls' Education.

At present there are seven universities in Saudi Arabia, which together have 67 colleges/institutes located in different parts of the Kingdom. In addition, there are 11 colleges and the Higher Institute for Social Work for girls (see table 4.2).

Table 4.2
Higher Education in Saudi Arabia key facts 1987/88

Category	Male	Female	Total
<u>Number of Students</u>			
University Colleges	66,700	27,663	94,363
Girls' Colleges	--	20,153	20,153
Total	66,700	47,816	114,516
<u>Number of Teachers</u>			
University Colleges	7,474	1,305	8,779
Girls Colleges	152	1,019	1,171
Total	7,626	2,324	9,950
<u>Number of Institutions</u>			
University Colleges*	67	--	67
Girls' Colleges**	--	11	11
Total	67	11	78

* Including Girls' Section

** Under the supervision of the General Presidency of Girls' Education.

Source: The Ministry of Higher Education [published in SAMA's Annual Report, 1988, p.119].

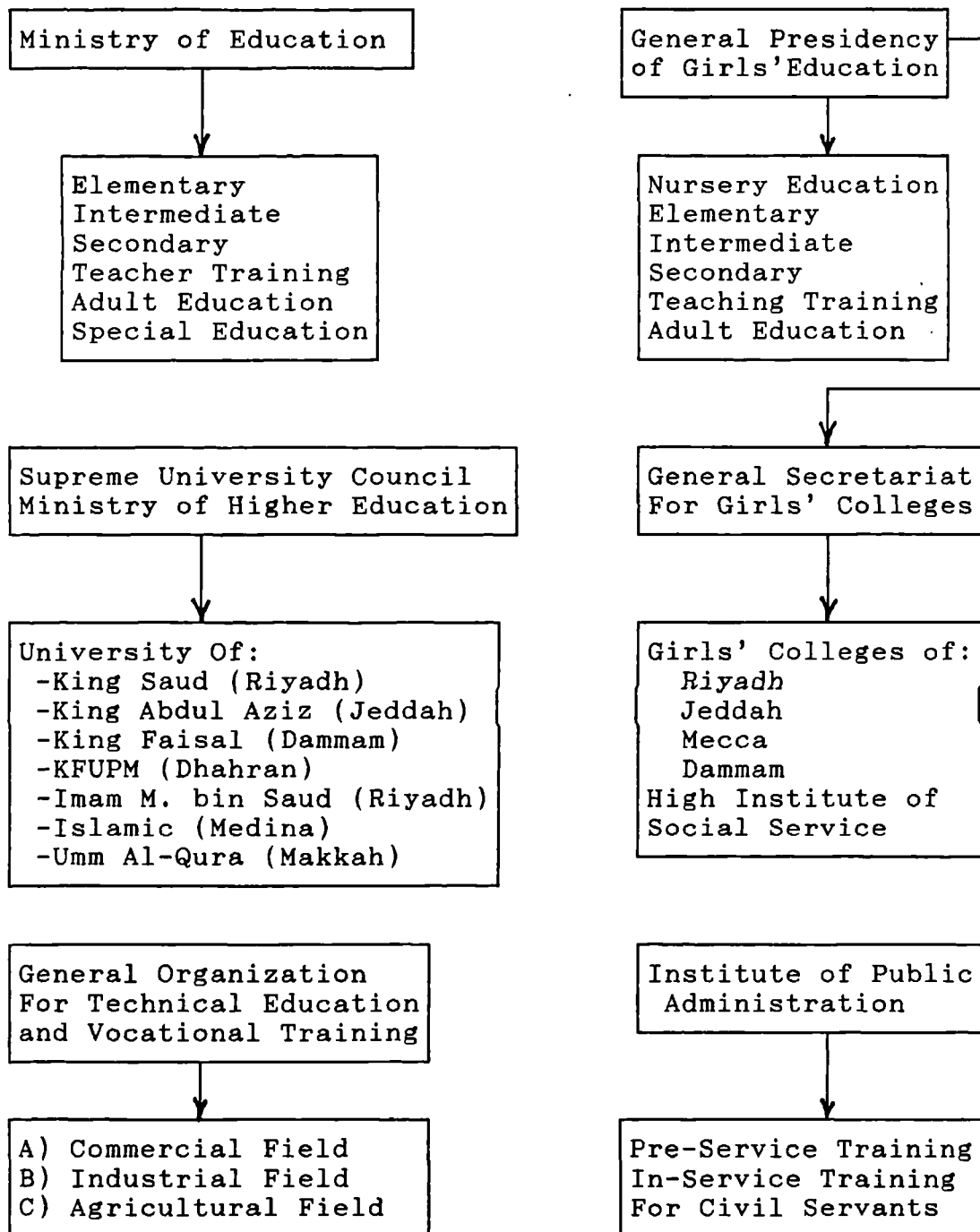
4.2.4 Educational Administration

The educational administration of Saudi Arabia is unique in that it is carried out by four main government authorities, namely: the Ministry of Education, the General Presidency of Girls' Education, the General Organization for Technical Education and Vocational Training, and the Ministry of Higher Education (see figure 4.1).

The Ministry of Education (MOE) has the overall responsibility for educational policy, curriculum, and organization of boys' education below the university level. It administers boys' schools at the pre-elementary and the first and second levels of general and vocational education for males.

The General Presidency of Girls' Education (GPGE) performs a similar function to that of the MOE, for females. The GPGE functions in close co-operation with the MOE and adopts an identical programme of studies with only slight adaptation suited to the special interests of girls' education. These two authorities (i.e. MOE and GPGE) control the education of almost 93 percent of the total male and female students in General Education (4DP, 1985-90, p.267). Each of them also administers teacher training institutes at the secondary level and junior teacher training colleges for male or female teachers. Education of the physically or mentally handicapped and adult education are also the direct concern of these two authorities.

Figure 4.1
The Structure of Education System in Saudi Arabia:
The Main Channels of Responsibility



Source: Modified and updated from Presley, J. (1984, p.116).

The General Organization for Technical Education and Vocational Training (GOTEVT), as its title suggests, is responsible for technical education and vocational

training. More specifically, the charter of GOTEVT defines its responsibilities as:

1. To promote Technical Education in the fields of industry, agriculture and commerce;
2. To upgrade standards at various levels to cover the trainees who are still in the preliminary stages, graduates, and those working in the public or private sectors;
3. To emphasize research and vocational studies aiming at the development of practical performance and the productivity of national manpower.

Prior to the establishment of the GOTEVT in 1980, technical education was the responsibility of the Ministry of Education.

The Ministry of Higher Education (MOHE) is responsible for the supervision, co-ordination and follow-up of higher education programmes and their linkage with the National Development programmes in different fields and for provision to the various sectors of the necessary technical and administrative manpower. The MOHE also operates educational missions outside the Kingdom to assist all Saudi students studying abroad and prepares statistical and evaluative reports about higher education. The MOHE was established in 1975. Prior to this date higher education was administered by the Ministry of Education.

Finally, the Institute of Public Administration (IPA) is an independent public authority, established in 1960 to provide courses for government employees in administration, personnel management and clerical and

secretarial skills. Its prime objective is to raise manpower efficiency in the public sector.

4.2.5 Financing of Education

Public education at all levels in Saudi Arabia is funded by the state, which provides education of all types and at all levels free of charge, to all citizens and residents. It establishes schools and provides such facilities as text-books and instructional materials, monthly allowances, free accommodation, transportation, and meals for students in technical and training schools and colleges.

Due to the rapid population growth and the government's commitment to free education, this sector can be expected to grow very rapidly during the 1990s. During the fifth development plan (1990-95), a total of SR 130,568 million will be allocated to the education sector (5DP, 1990-95, p.273). This excludes vocational and technical education and training which will be allocated SR 7,015 million (Ibid. p.285).

To sum up, the formal system of public education in Saudi Arabia is a single track system founded on six years of elementary and three years of intermediate schooling. This is followed by three years of secondary school and four years (or five years in the case of Engineering and Medicine) of college education. This single track may be lengthened by pre-elementary kindergarten and postgraduate study. Education at all levels for all citizens and residents is provided free of

charge and, in keeping with the tenets of Islam, strict segregation of the sexes is maintained in all educational institutions.

4.3 Accounting Education Below University Level

In spite of its rapid economic development, Saudi Arabia is still suffering from a shortage of skilled manpower. As the government is aware of this shortage, the attention of national development planning has been devoted to vocational and technical education. The establishment of Secondary Commercial Schools and the Higher Institutes for Commercial and Financial Sciences to meet the increasing need for bookkeepers, administrators, secretaries, and clerks for both government agencies and private institutions, exemplifies this.

4.3.1 Secondary Commercial Schools

In 1971/72, the first three secondary commercial schools were established in Riyadh, Jeddah and Damamm with a total enrollment of 180 students (GOTEVT, 1988, p.3). By the end of 1987/88, there were eleven secondary commercial schools throughout the Kingdom, with a total of 7.755 students (see table 4.3).

To be admitted to one of the secondary commercial school, the candidate must hold the intermediate school certificate. The secondary commercial schools run two sessions, one in the morning and the other in the evening. The evening session is designed to enable those

Table 4.3
Secondary Commercial Schools
Number of Students and Graduates
1980 - 1988

Year	No. of Students	No. of Graduates
1980/81	4468	1074
1981/82	4936	1206
1982/83	5828	1305
1983/84	6479	1520
1984/85	6352	1647
1985/86	8548	1671
1986/87	7383	1474
1987/88	7755	N/A
Total	51749	9897

Source: GOTEVT Statistical Report, Several Issues.

in employment to attend. As with all GOTEVT schools and institutes, students in the morning session are offered a monthly grant to cover their personal expenses; only those aged between 15 and 18 years are admitted to the morning session.

The duration of study in these schools is three years, after which the graduate is granted the Secondary Commercial Certificate. The basic components of the programme of study are as follows (GOTEVT, 1988, p.12):

1. Accounting and Book-keeping;
2. Administration and Secretarial;
3. Commercial Correspondence and Typing.
4. Banking Transactions.
5. Purchasing and Warehousing.
6. Sale and Purchase Transactions in Local and Foreign Trade.
7. Collection and Cash Affairs.

8. Computer Programming (introduced recently in one school only, i.e. Quatif Secondary Commercial School).

4.3.2 The Higher Institute for Commercial and Financial Sciences.

There are two Higher Institutes for commercial and financial sciences in Saudi Arabia, one in Riyadh (established in 1975/76) and the other in Jeddah (established in 1977/78). As in the case of secondary commercial schools, both of these institutions hold morning and evening sessions. The programme of study is divided into two sections (Ibid):

1. Accounting and financial section: including government accounting, bank accounting, cost accounting, and petroleum accounting.
2. Business Administration section: including industrial management, social insurance, staff affairs, purchasing, and warehousing.

Candidates for admission to these institutions who have graduated from Secondary Commercial Schools can join any section, but holders of the Secondary General Schools Certificate can only join the secretarial section. Duration of study is two years, after which the graduate is granted a Higher Diploma in Commercial and Financial Science.

In order to motivate students to join these institutions, students in the morning session are offered a monthly grant in addition to free accommodation, transportation and meals. Table 4.4 shows the number of students and graduates in these institutes.

Table 4.4
The Higher Institute for Commercial
and Financial Sciences
Number of Students and Graduates
1980 - 1988

Year	No. of Students	No. of Graduates
1980/81	292	78
1981/82	229	78
1982/83	271	99
1983/84	256	83
1984/85	330	84
1985/86	310	114
1986/87	439	131
1987/88	542	N/A
Total	2669	667

Source: GOTEVT Statistical Report, Several Issues.

4.4 University Accounting Education, with Special Reference to King Abdul Aziz University

The College of Administrative Science (formerly known as the College of Commerce) at King Saud University (KSU) was the first institution of higher education to offer a business curriculum in Saudi Arabia. Study at this institution began in the autumn of 1959. This was followed by the establishment of the College of Economics and Administration at King Abdul Aziz University (KAU) in 1967 and the College of Industrial Management at the University of Petroleum and Minerals (UPM)² in 1974. All three institutions offer undergraduate as well as postgraduate courses in accounting (Abdeen and Yavas, 1985). In addition, there are two other universities (King Faisal and Umm Al-Qura) in Saudi Arabia introduced undergraduate accounting courses in recent years.

² This University has been recently renamed as King Fahad University for Petroleum and Minerals (KFUPM).

4.4.1 Undergraduate Programme

To be admitted to the undergraduate programme leading to a bachelor degree in accountancy, the candidate must hold either the secondary general or the secondary commercial school certificate. However, admission for the latter is restricted to those who graduate with an excellent grade. To obtain the degree of bachelor majoring in accounting, the candidate must successfully complete the required courses and present a project on any topic related to accounting.

The overall requirements for the bachelor degree in accounting are relatively varied among Saudi universities. For example, the student is required to complete successfully a total of 129 credit hours at KSU and 132 at KFUPM (Ibid. p.165), while a recent revision of the accounting curriculum at KAU aiming to upgrade accounting education, has lengthened the accounting programme for the bachelor degree from 126 to 136 credit hours. The overall programme of study is divided into six parts, of which 51 (37.5%) credit hours are pure accounting courses (see table 4.5).

Despite this recent revision, some problems related to the accounting curriculum remain unresolved. One problem, for example, relates to the need to expose students to practical experience in order to narrow the gap between the theoretical training and its practical application.

Table 4.5
Requirements For Bachelor Degree In Accounting:
King Abdul Aziz University (The New Plan)

(1) Compulsory Courses Required by University Regulation (14 Hours)

<u>Name of the Courses</u>	<u>C/H*</u>
1. Islamic Studies	2
2. Islamic Studies	2
3. Islamic Studies	2
4. Islamic Studies	2
5. Arabic Language	3
6. Arabic Language	3
	--
	14
	==

(2) Compulsory Courses Required For the Faculty (54 Hours)

1. Principles of Scientific Research	1
2. Principles of Business Administration	4
3. Principles of Public Administration	4
4. Principles of Economics	3
5. Principles of Accounting	3
6. Principles of Political Science	3
7. Principles of Mathematics	3
8. Principles of Statistics	3
9. Principles of Law	3
10. Principles of Economics	3
11. Principles of Accounting	3
12. Principles of Computer Science	3
13. Principles of Quantitative Analysis	3
14. English Languages	3
15. Saudi Arabia Political System	2
16. Organizational Behavior	2
17. Fundamentals of Islamic Administration.	2
18. Fundamentals of Islamic Economics	2
19. Zakat Accounting	2
20. Petroleum Economics	2
	--
	54
	==

(3) Compulsory Courses Required For the Accounting Department (35 Hours)

1. Partnership Accounting	3
2. Corporate Accounting	3
3. Principles of Cost Accounting	3
4. Principles of Auditing	3
5. Tax Accounting	2
6. Governmental Accounting	3
7. Advanced Financial Accounting	3

Table 4.5 (continued)

8. Cost Accounting	3
9. Managerial Accounting	3
10. Petroleum Accounting	2
11. Accounting Information System	2
12. Auditing and Investigation	3
13. Research Seminar (Accounting)	2
	--
	35
	==
(4) <u>Elective Courses Required From the Accounting Department (9 Hours From the Following for Male and 6 Hours for Females)</u>	
1. Specialized Institutions Accounting	3
2. Computer Application in Accounting & Auditing	3
3. Accounting System in Islam	3
4. Readings in Accounting (In English)	3
5. International Accounting	3
6. Accounting Theory	3
7. Accounting and Financial Analysis	3
8. Government Auditing and Investigation	3
9. Apprenticeship	3
	--
	27
	==
(5) <u>Compulsory Courses Required From Other Departments (15 Hours)</u>	
1. Programming Languages	3
2. Money and Banking	3
3. Commercial Law	3
4. Financial Management	3
5. Econometrics 1	3
	--
	15
	==
(6) <u>Free Courses (9 hours for Males and 12 for Females)</u>	

* C/H --> Credit Hours

Source: Students Guide for Accounting Department, Faculty of Economic and Administration, King Abdul Aziz University, Jeddah, 1988, p. 28-29

Another problem relates to the emphasis upon private sector accounting rather than public sector accounting, despite the small size of the former compared with the

latter. Evidence of such emphasis can be seen easily from a close look at the programme contents (see table 4.5) which reveals that most of the subjects are related to external reporting and external auditing, even though internal auditing is at least as important as, and perhaps more important than, external auditing in the Saudi Arabian environment. Further, more time is spent on financial accounting than on cost/management accounting. Yet the success of the Saudi Arabian economy will depend, among other things, upon the effectiveness of management and the decision-making processes which depend so heavily on cost/management accounting techniques and ideas; for example, the budgeting process (including performance budgeting for government), setting sound standards of performance and the related evaluation of performance, cost-benefit analysis, and sound project appraisal.

On average, students are expected to graduate after four years (eight semesters). Student performance throughout the programme is evaluated according to a points scale, ranging from F (Fail) - zero points, to A (excellent) - five points (see table 4.6).³

³ It should be noted that according to the very recent Resolution of the Council of Ministers (1992), the credit hours system will be abolished in all Saudi universities and colleges of higher education starting from the academic year 1413H (1993) and will be replaced by the traditional system (i.e. studying on yearly basis).

Table 4.6
Registration of Student's mark in each course

Marks	Points	Grades
From 90 to 100	(4-5)	A (Excellent)
From 80 to less than 90	(3.0-3.9)	B (Very Good)
From 70 to less than 80	(2.0-2.9)	C (Good)
From 60 to less than 70	(1.0-1.9)	D (Pass)
From 0 to less than 60	Zero	F (Fail)

Source: Students Guide, op. cit. p.60

The 100 marks for each course are distributed as follows (Science Guide, 1988, p. 59):

- Mid-semester test	20 Marks
- End of semester test	40 Marks
- Course work during a semester	40 Marks

- Total	100
	===

Sixty is the minimum mark to pass the course. However, for any student to graduate he or she has to earn an overall average of at least C grade, or two points.

Table 4.7 shows the number of students graduating from the accounting department, KAU, since it was established fifteen years ago. The number reached 1,301 graduates in 1989/90.

Table 4.7
King Abdul Aziz University, Accounting Department
Number of Graduate in Accounting, 1971/72 -1989/90

Year	No. of Graduates in Accounting
1971/72	--
1972/73	--
1973/74	--
1974/75	8
1975/76	62
1976/77	42
1977/78	58
1978/79	63
1979/80	49
1980/81	95
1981/82	100
1982/83	99
1983/84	140
1984/85	132
1985/86	138
1986/87	90
1987/88	111
1988/89	114
Total	1301

Source: Accounting Department, Annual Report 1410 H. (1990), King Abdul Aziz University, Jeddah, Saudi Arabia.

4.4.2 Postgraduate Programme

There are three universities in Saudi Arabia currently offer a postgraduate programme leading to a Masters degree in accounting. To be admitted the candidate must possess the Bachelor degree. As in the case of the undergraduate programme, the length and the contents of postgraduate programme vary among Saudi universities.

The postgraduate programme leading to the Master degree in accounting at KAU began in the 1976/77. The programme of study consists of 36 credit hours divided into two main parts (Students Guide, 1988, p.69).

The first part is course-work and constitutes 27 (75% of the overall requirements) credit hours of which 15 are advanced courses in accounting, while the remaining 12 are advanced courses in business and economics.

The second part is a written dissertation which accounts for 9 credit hours. The topic may be in any accounting area. After the completion of the dissertation, it must be defended before three academics, of whom one should be an external examiner from another institute.

On average, students are expected to graduate after three years (six semesters). However, the dissertation sometimes takes longer than expected, partly due to the amendment of the research topic or because of the terms of the student's supervisor's contract (in the case of non-Saudi professors). The evaluation of the student's performance during the course-work is similar to that of the undergraduate programme, i.e according to a points scale (see section 4.4.1).

Table 4.8 shows the details of the programme leading to the Master degree in accounting currently offered by KAU.

Table 4.8
Requirements For Master Degree in Accounting
King Abdul Aziz University

(1) Compulsory Courses (21 Hours)

<u>Name of the Courses</u>	<u>C/H*</u>
1. Contemporary Business Environment in Saudi Arabia	3
2. Research Methodology in Business	3
3. Quantitative Analysis Methods	3
4. Accounting Theory	3
5. Managerial Accounting	3
6. Auditing Theory	3
7. Managerial Economics	3
	--
	21
	==

(2) Elective Courses (6 Hours)

The student has to choose, with the guidance of his Academic Advisor, two courses constituting six semester credit hours of which Costing Theory must be studied.

1. Behavioral Approach in Accounting	3
2. Public Accounting	3
3. Social Accounting	3
4. Cost Theory	3
5. Cost Analysis and Control	3
6. Auditing Cases & Investigation	3
7. Accounting Theory in Islam	3
8. Zakat and Taxation	3

(3) Dissertation (Constitutes 9 Credit Hours)

* C/H --> Credit Hours

Source: Students Guide, op. cit. p.72

4.4.3 Accounting Teachers

The following posts and qualifications are common to all universities in Saudi Arabia (Regulations and Bylaws of King Abdul Aziz University, 1985, pp.141-42):

- (1) Teaching Assistant: qualification is B.A. in Accounting with minimum very good (B) grade plus a successful interview conducted by a

special academic committee formed for this purpose.

- (2) Lecturer: qualification is the Master degree or equivalent from any recognized academic institution.
- (3) Assistant professor: qualification is a doctorate from any recognized academic institution.
- (4) Associate Professor: qualification is the same as for assistant professor above, plus at least four years experience and publications.
- (5) Professor: qualification is the same as for assistant professor, plus at least eight years experience and publications, with at least four in the post of associate professor.

The doctoral degree is a requirement for a permanent teaching position in all universities in Saudi Arabia. No professional qualification is required, as it is not accepted as a basis for appointing lecturers. However, appointment of a master' degree holder as a lecturer has been postponed in recent years on the grounds that those concerned should be encouraged to pursue their higher education in order to obtain their Ph.D Degree.

Table 4.9 shows the number of full-time accounting Faculty in King Abdul Aziz University by rank and nationality.

Table 4.9
 Characteristics of Full-Time Accounting Faculty
 At King Abdul Aziz University (1989-90)

Academic Rank	Nationality		Total
	Saudi	Non-Saudi*	
Professor	--	3	3
Associate Professor	3	7	10
Assistant Professor	6	1	7
Lecturer **	11	2	13
Teaching Assistant	4	-	4
Total	24	13	37

* Currently all non-Saudi are Egyptians.

** All Saudi lecturers serve as teaching assistants.

Source: Compiled by the author from the Annual Report for the 1410 H. (1990) Academic Year, Accounting Department, King Abdul Aziz University, pp.22-23.

Currently, all accounting teachers are full-time, with a minimum level of twelve hours' class teaching per week. However, because of the large number of accounting students, particularly in recent years, most of the staff members of accounting departments have to carry an extra teaching load.⁴

4.4.4 Teaching Methods and Techniques

Lectures combined with blackboard demonstration and textbook assignments are the most commonly used teaching methods in Saudi Arabia. The traditional accounting lecture is given in a large classroom with the total number of students exceeding eighty in some courses, particularly in the compulsory courses.

⁴ According to the latest report, the ratio of Faculty members to students was 1 to 51 (Accounting Department, KAU, Annual Report, 1990, p. 24).

Arabic is the language of study in the accounting department in KSU and KAU, while UPM uses both Arabic and English. In KSU and KAU most of the Arabic textbooks have been imported from Egypt, and only a few accounting textbooks have been written by Saudi Faculty members (Abdeen and Yavas, 1985).

Perhaps the most remarkable feature of accounting education in Saudi Arabia is the emphasis upon theory, and the disregard for practical techniques. However, less emphasis is placed on developing critical analysis, reflective thinking, and independent judgement. Moreover, the use of the library is not common since term papers are not required in most undergraduate programmes.

Hence it is widely believed that more innovative teaching techniques and approaches should be adopted so that students are motivated to think for themselves and to continue their pursuit of knowledge, even beyond the end of their formal education.

4.5 Some Problem Areas in Accounting Education

4.5.1 Computer Accounting Education

It is safe to say that computer accounting education in Saudi Arabia is not what it ought to be. For example, under the current plan of accounting programme at KAU, only one course deals with computer accounting, and even this course is found among the electives (see table 4.5). Moreover, to the best of the author's knowledge, none of the current accounting staff members (either Saudi or

non-Saudi) at KAU has any interest in computer accounting.

4.5.2 Textbooks

The lack of proper accounting textbooks is an additional problem facing accounting education in Saudi Arabia, in terms of quality as well as quantity. Currently most textbooks are Egyptian, in the case of KSU and KAU, and American in the case of UPM. Abdeen and Yavas (1985, p.169), both of whom are associate professors in Saudi universities, have criticized the quality as well as the relevance of such textbooks to Saudi Arabia's socioeconomic environment, they argue:

"A wide disparity exists in the quality of these texts [accounting texts], and a critical review suggests that they deal with Egyptian business, social security tax laws, and auditing and accounting standards, which differ from those practiced in Saudi Arabia. At UPM, American textbooks are widely used. Both the Arabic and American textbooks suffer from the same problem, however: they are not written with Saudi Arabia in mind."

It must be mentioned, however, that the influence of Egyptian textbooks upon the education system in Saudi Arabia has a long history. This fact was pointed out by Abdul-Wassie (1970, p.23) when he said:

"Our education policy has for many years been closely linked with that of our neighboring Arab countries (mainly Egypt). We adopted their organization, their curricula and their textbooks to ensure that the graduates from our secondary schools should be able to gain admission to their universities at a time when Saudi Arabia had no universities of its own."

In attempts to overcome the shortages of accounting textbooks, a few American textbooks have been translated into Arabic by KSU faculty staff in recent years. However, these texts suffer from certain problems mainly due to differences in terminology between English and Arabic.

It seems desirable that accounting textbooks in Saudi Arabia, as in other developing countries, should be written on an original basis, with reference to American and European books in the areas of quantitative techniques, but not in areas of accounting practice. The blind importation of foreign concepts and theories may cause more problems in real situations and may be irrelevant to the Saudi Arabia socioeconomic environment.

Because the textbook is a prerequisite for the development of curriculum and better teaching, the textbook problem must be solved together with the problems of curriculum and teaching materials.

4.5.3 Lack of Research

Research is usually recognized to be one of the principal duties of academic departments at universities. Nevertheless, accounting research in Saudi Arabia has been limited, mainly for lack of free time for accounting instructors. The main reason behind this is the heavy teaching loads of about 12 hours per week.

Generally speaking, the lack of research in general and accounting in particular is not unique to Saudi Arabia but a common phenomenon in many developing

countries. This is very clear from the following observations of Enthoven (1981, p.54):

"In most [developing] countries research and development activities are extremely weak. Both the funds and well-qualified personnel are scarce, and the regular accounting practitioners at both government and private levels are too occupied with daily tasks. In many instances, accounting research and related functional developments are limited to copying foreign accounting research and pronouncements without effectively determining domestic relevancy."

Nevertheless, the significance of research and development has been recognized by the government of Saudi Arabia in recent years. The establishment of King Abdul Aziz City for Science and Technology (KACST) can be set as an example of this. The KACST is an independent scientific organization, administratively attached to the Council of Ministers. According to its charter, the KACST suggests the national policy for developing science and technology and drawing up strategy and plans for implementation. It is concerned with the implementation of applied science research programmes and assisting the private sector in research and development of agricultural and industry products. It also supports joint research programmes between the Kingdom and international scientific institutions.

It is clear that the efforts of KACST are directed toward science subjects and there is no evidence that it has carried out or supported any accounting research so far.

Furthermore, there are as yet no specialized accounting journals in Saudi Arabia which could enhance accounting research. However, there are three general business journals which include a few accounting articles. They are:

1. *Public Administration*, published by the Institute of Public Administration, Riyadh.

2. *Journal of Economics and Administration*, published by Research and Development Center, King Abdul Aziz University, Jeddah;⁵

3. *Journal of the Faculty of Commerce*, King Saud University, published by King Saud University Libraries, Riyadh.

The accounting articles are published in Arabic and English (sometimes only in abstract) in the above journals and furnish a forum for academics and professionals to exchange views on matters of professional interest.

In addition to the above journals, some articles related to accounting problems have been published in the local newspapers (currently seven) as well as other weekly magazines such as AL-YAMAMAH.

⁵ This Journal ceased publication for several years and was republished recently under slightly different name and covered

4.6 Summary and Conclusion

The main purpose of this chapter has been to present a broad and objective picture of the development of accounting education in Saudi Arabia. Basically, accounting education operates within the framework of the education system of the country as a whole.

This education system has two distinct characteristics: traditional, which emphasizes Islamic teachings and principles and stresses the Saudi Arabian role as the preserver and protector of Islam; and the focus on Western institutions, methods and technological innovations as a means of improving Saudi Arabian society.

Accounting education in Saudi Arabia consists of two main levels, sub-university and university level. The former includes the secondary commercial schools as well as the Higher Institutes for Commercial and Financial Science, while the latter includes university colleges which provide undergraduate and postgraduate programmes in accounting.

The present university undergraduate accounting programme leading to the B.A. degree, and the graduate programme leading to the M.Sc. degree seem to be adequate, compared with similar programmes in other developing countries. Moreover, many graduates of these programmes have been admitted to postgraduate accounting programmes in developed countries such as USA and UK.

CHAPTER 5

ACCOUNTING PROFESSION IN SAUDI ARABIA

5.1 Introduction

The aim of this chapter is to discuss the main features of the accounting profession in Saudi Arabia. The chapter is divided into two main parts: the first part provides a brief historical background to accounting with special reference to the accounting system found in the early Islamic State and its links with the current accounting system and practice in Saudi Arabia. This part also reviews the development of accounting practice in Saudi Arabia in three distinct phases and highlights the main features of the new proposed Law of Certified Accountants. Environmental factors which might affect accounting practice in Saudi Arabia are also discussed in this part.

The second part is devoted to the analysis and discussion of the empirical survey which has been conducted in Saudi Arabia. The aim of this was to contribute to better understanding of some practical aspects of current accounting practices in the Kingdom.

5.2 Historical Background to Accounting

An awareness of its background helps in understanding any discipline. Therefore, the purpose of this section is to explain briefly the historical background to accounting with particular reference to the system found in the early Islamic State, because it has

several links with the current accounting system and practice in Saudi Arabia.

Accounting is known to have been practised since early times, and has developed with the passage of time through many stages. Different records for different purposes have been used during these stages. For example, clay tablets were used by the Babylonians and Assyrians; the ancient Egyptians used papyrus to record their transactions. Moreover, the need to keep records of financial and other business transactions is an ancient one. It is thought that the earliest scripts go back to Assyrian and Babylonian times.

"Many examples have been found of early attempts to record business transactions. There are records of such transactions in Assyria as early as 3500 B.C.; clay tablets were found in Babylon dating back to 2300 B.C.; and records were found in Egypt which relate to the building of the pyramids." [Briston, 1981, p.4]

In the past, economic activities were very limited. Thus the volume of transactions was relatively small and the settlement of such transactions was usually carried out under a barter system, since there was no monetary unit. In addition, resources used in business were owned by individuals who were also involved in the day-to-day operations of their business. There was no double-entry system as known in modern times. As a result, receipts and expenditure were usually kept in separate sheets rather than in the form of debit and credit (Ibid).

Accounting was also known in classical times. The practical applications of accounting in ancient Greece and Rome have been recognized by many accounting historians (de Ste. Croix, 1956; Costouros, 1977).

Financial records improved through the centuries, and their importance has been widely recognized. For example, with the establishment of the Islamic State in the seventh century, financial affairs were given more attention. Islam requires the two parties, creditor and debtor, when dealing with each other, to set down in writing the details of their transaction, in front of two witnesses. God says in the Holy Qur'an (chapter II. para 282):

"Ye who believe! when ye deal with each other, in transactions involving future obligations in a fixed period of time, reduce them to Writing. Let a scribe write down faithfully as between the parties: let not the scribe refuse to write: as God has taught him, so let him write, let him who incurs the liability dictate, but let him fear his Lord God, and not diminish aught of what he owes".

Much later in Italy, the introduction of the double-entry book-keeping system by the end of fifteenth century was considered as the highest stage of the development of accounting at that time. In 1494, Pacioli, an Italian mathematician, published a book which included a section on the double-entry book-keeping system. Although the name of Pacioli is associated with the introduction of the double-entry system, there was a strong relationship between the emergence of the system and the expansion of

commerce which occurred in Italy in the period from around the middle of the 13th to the 14th century. Evidence of such relationships can be seen in the formation of partnerships and the growth of the commercial banks during the period concerned. In addition to that, Pacioli said himself that the double-entry system was much older (Have, 1986, p.10).

Littleton (1981, p.13) pointed out the unique and important antecedents essential to the development of double-entry book-keeping. These include Material (something which needs to be reworked), Language (a medium for expressing the material), and Methodology (a plan for systematically rendering the Material in the Language).

The Industrial Revolution, especially in the United Kingdom, marked a new phase in the history of accounting. The huge and sudden expansion of commerce resulted in tremendous growth in the number of business entities and consequently the volume of transactions. These factors and others, such as the establishment of Joint Stock Companies and the separation between management and ownership, led to an increase in the demand for book-keeping services. New records and technical procedures were used to handle financial transactions in these business entities. The influence of the Industrial Revolution on the development of bookkeeping is well articulated by Have (1986, p.16):

"First, the Industrial Revolution made new demands on the bookkeeping system, and secondly, it influenced bookkeeping. ... The typewriter, the adding machine, and, finally, the bookkeeping machine again influenced accounting techniques; also the introduction of the punched card system ... The advent of the computer once again influenced the bookkeeping techniques".

Other factors have contributed to the development of accounting. For example, the establishment of professional societies during the second half of the nineteenth century was considered as one of the major factors that influenced the development of accounting. The first of such societies was established in Scotland in 1854, followed by the English Institute in 1880. These professional societies provided education and training programmes for their members. They also contributed to the spread of accounting all over the world, due to the spread of their membership.

To sum up, bookkeeping, and, later, accounting, have developed continuously through different stages to meet the changing needs of society. The function of accounting has also changed from a mere tool for calculation to an independent subject having its own theory and practice. However, study of the development of accounting in each different stage is beyond the scope of this research. Nevertheless, it is appropriate to throw some light on the accounting system in the early Islamic State, since there is an inherent link between that system and the current accounting system and practice in Saudi Arabia. Consequently, the following two sub-sections discuss the

accounting system in the early Islamic State and briefly explain this link.

5.2.1 Accounting Systems in Islam

According to Islamic Sharia (law), accounting is a science which looks into the accounting of equities and liabilities in the light of Islamic Sharia, which includes rules in *Abadats* (worship) and *Mo'amalat* (dealings). [Tarabzoni, 1985, p.22].

The early Islamic State was established with the emergence of Islam in Arabia (Makkah), Saudi Arabia today, in 610 A.D. At that time commerce was the major activity of the population. Makkah, beside being the holiest city, served as a commercial centre of the region. Pilgrims came to Makkah from different parts of the world, carrying with them different kinds of monetary means, usually in the form of gold, silver, and other valuable metals. Every year, they exchanged their monetary means for the goods and services provided there (El-Ashker, 1987, p.11).

Islam permits trade but prohibits usury or *Riba*¹. It sets rules to govern people's dealings with each other. Among these rules, as mentioned earlier, is the requirement that transactions between parties be put in writing. Moreover, *Zakat* is imposed on the wealth and income of rich people and distributed to particular

¹ *Riba*: literally means increase or addition and refers to the 'Premium' that must be paid by the borrower to the lender along with the principal amount as a condition for the loan or an extension to its maturity (Chapra, M.U., 1986, p.263).

categories of people specified in the Qur'an. The Prophet himself employed people to collect zakat and charity and required all these funds to be recorded in writing for the purpose of accountability.

The early Muslims gave particular attention to accounting in the public sector. The establishment of the "Bayt-al-Mal" can be cited as an example. "Bayt-al-Mal" is a public organisation similar in its function to what is known today as the State Treasury. Its main objective was to control the income and expenditure of the state at that time. As El-Ashker (1987, p.13) states:

"Financially, he [the Prophet] established the Treasury, "Bayt-al-Mal", which was headed by a treasurer appointed by the head of state. The treasurer was responsible for controlling items of revenue and expense and was to exercise his duties and authority in conformation with Qur'anic rules and the Prophet's instructions."

The expansion of the Islamic State and consequently the increase of economic activities led to the establishment of new branches of "Bayt-al-Mal" in different parts of the State, each of which was headed by an independent local treasurer, whose responsibilities are described by El-Ashker as follows:

"A local treasury was established in each province (Egypt, Iraq, Syria, etc.) and was headed by a treasurer - who was not the province's governor - appointed by the head of the state. The treasurer was responsible for the province's revenues and expenditure and was accountable to the head of the state in the state's capital. While general policies were laid down centrally by the head of the state, authority was delegated to local treasurers to

exercise their duties on a decentralized basis. Local treasurers were not delegated any authority, however, to add or alter taxes without the prior consent of the head of the state". [Ibid. p.17].

Various languages were used in recording financial transactions in these branches, depending upon the local language of the province in which the branch was located. Later, however, these differences were unified and Arabic became the main language used in all transactions. [Ateyah, 1982, p. 33].

The main sources of revenues and expenditure of the "Bayt-al-Mal" can be summarized as follows (Ibid, p.34-37):

Revenues

1. Al Zakat (Religious tax);
2. Al Kharj (Taxes levied on land);
3. Al Jizyah (Taxes levied on non-Muslims in lieu of military service);
4. Al Kaniam (benefit won during war, such as horses, military equipment, etc.);
5. Al Osher (the tithe = a tenth of one's income); and
6. Others.

Expenditure

1. Payment of zakat to the categories specified in the Qur'an: "The poor, the pauper, the people who collect it, the new convert, the liberation of slaves, the indebted, in the cause of God and the wayfarer" (Qur'an, IX:60);

2. Salaries of soldiers. The amount of salaries was determined by Umar (the second Caliph) according to the types of duty attached to each soldier as follows: 7000, 8000, 9000 Dirhams (i.e monetary unit used at that time) annually;
3. Salaries of Judges, Governors and other administrative officers. The amount of salary here was determined by the recipient's previous experience in Islam. For example, 5000 Dirhams were paid for those who had witnessed the battle of Badar (the first battle in Islam), 4000 Dirhams for old Muslims, and 3000 Dirhams for the sons of immigrants and Anssar (residents of Medina at that time);
4. Agricultural expenditure, such as irrigation and digging wells;
5. Prisoners' expenses such as food, drink and clothes;
6. Expenditure on military equipment;
7. Gifts and Grants for Artists and Alama (intelligent people).

At the end of each fiscal year, the total revenue was compared with the total expenditure in order to compute the surplus (or deficit) of the "Bayt-al-Mal". This involved actual investigation to ensure the accuracy of the accounting records. Such action, according to Ateyah, was similar to internal control at the present time (Ibid, p. 37).

From the preceding discussion, it can be concluded that the imposition of Zakat and the related activities

such as assessment, collection and distribution; and the establishment of the "Bayt-al-Mal", might all be considered as an indication of the need for a good accounting system in the early Islamic State.

5.2.2 Inherited Links

The existence of a historical link between the accounting system found in the early Islamic State and the current system in Saudi Arabia can perhaps be seen through two main historical features, the imposition of Zakat and the prohibition of Riba.

The imposition of Zakat and its related activities (e.g. assessment, collection, and distribution) which were practised in the early Islamic State, are still practised in Saudi Arabia today. Indeed, there is a special government department called the Zakat and Income Tax Department (ZITD) which was established within the Ministry of Finance and National Economy in 1950. The main function of ZITD is to assess and collect Zakat from Saudi citizens and Tax from foreigners. Moreover, Zakat appears as a separate item in the revenues side of the current budget classification of Saudi Arabia (see chapter 7).

Also the prohibition of interest which was introduced by the early Islamic financial system, is still observed by the Saudi Government. Evidence of this can be seen in the establishment of a number of financial institutions which provide short as well as long term loans to Saudi citizens without charging interest.

Examples of these institutions are: Saudi Industrial Development Fund (SIDF), Saudi Real State Bank (SRSB), Saudi Credit Bank (SCB) and Saudi Agricultural Bank (SAB). In addition, it was clearly stated in the Charter of the Saudi Arabia Monetary Agency (SAMA), the central bank and the apex of the Saudi financial system, that (Art. 7):

"The agency shall not charge any profits on its receipts and payments and shall not act in a manner which conflicts with the teachings of the Islamic law. The Agency shall not undertake any of the following:

a) paying or receiving interest; ..."

Furthermore, the accounting education system (see chapter 4) was designed to maintain Islamic principles. For example, the current accounting programme which is provided by King Abdul Aziz University includes two courses dealing with the above issues. One such course is "Zakat Accounting", which deals with the interpretation and application of the Islamic principles in Zakat which includes: comparative study between Zakat and Taxes, persons and properties liable to Zakat, and Zakat of Agricultural Crops and Funds. Another course, entitled "Accounting System in Islam", has as its objective the study of the financial and accounting systems in Islam, including the scientific concept of accounting in Islam and its rules for accounting measurements, planning, decision-making, and inheritance.

5.3 The Development of Accounting Practice in Saudi Arabia

The development of accounting in Saudi Arabia may be discussed under three phases: (1) The phase before the passing of the 1974 Law of Certified Accountants; (2) accounting practice under the 1974 Law of Certified Accountants; and (3) Recent Developments (1986 to the present).

5.3.1 Accounting Practice prior to 1974

As explained in chapter three, prior to the discovery of oil in 1938, Saudi Arabian's economy was poor and depended mainly upon income received from pilgrims to the Holy Cities (i.e Makkah and Medina) and various traditional business activities. These activities were normally dominated by one person or family, who owned all the resources used and was completely involved in the day-to-day operations of the business. Little attention was given to accounting records, and even where these were kept, it was on a primitive and single-entry basis (Shinawi, 1970, p.37).

In addition, there was no notable industry, a lack of capital accumulation, and few skilled workers or experienced entrepreneurs. At that time the resources of the country were directed towards the establishment of administrative organisations and the development of communications, education, security and medical facilities.

The discovery of oil in abundant quantities has made Saudi Arabia a wealthy country with all modern amenities.

Since the first exports of crude oil began in 1939, this commodity has become the dominant feature of the economy, providing more than 90 percent of government revenues in the fiscal year 1980/81 (SAMA's Annual Report, 1986, p.32).

The need for accounting information emerged with the changes in economic and commercial activities in Saudi Arabia. With the growth of corporations and the separation between management and ownership, the need for better accounting services increased. Management needs accounting information for rational decision-making, while investors, creditors (mainly commercial banks) and government (Zakat and Income Tax Department) are interested in the financial position and results of operations of corporations in the Kingdom.

In 1955, the first accounting firm was established, a foreign firm known as "Saba, Nawar, and Co." At that time, the authority to issue an accountant's licence was exercised by the Ministry of Finance and National Economy. In 1957, that authority was transferred to the Ministry of Commerce and Industry. The first Saudi accounting firm was established in 1959, known as "Al-Daghastani and Abdul Wahab". By the end of the 1950s there were only seven accounting firms in Saudi Arabia (Ba-Eissa, 1984, P.301).

Although the first accounting firm was established in 1955, this does not mean that there was no accounting practice in Saudi Arabia before that date. Ba-Eissa, for

example, found that the attestation function was used by some companies in Saudi Arabia from 1948 (Ibid. P.302).

In 1961 the Companies Act was drafted and offered for public discussion and debate (Shinawi, 1970, p.41). However, the draft was initially rejected because, according to Shinawi, it "was almost an exact copy of the Egyptian law 26 of 1954, except for minor changes such as doubling the amounts of fines and assigning the Ministry of Commerce and Industry to take the place of the Egyptian court in settling disputes". This Egyptian influence may be ascribed to the fact that most of the committee members responsible for the preparation of the draft were Egyptian legal advisers and even the Saudi nationals among the committee members had received their education in Egypt (Ibid).

The review and discussion of the Companies Act draft continued for about four years until it was finally enacted in 1965. The Act, which is still in effect, was the first statute to recognize the accounting profession in Saudi Arabia. It includes some accounting guidelines, particularly in respect of the appointment of the auditor, his duties, rights and responsibilities (see chapter 3). The Act also requires the Board of Directors to prepare the balance sheet, and the profit and loss account, and to make them available to the auditor at least fifty-five days before the Annual General Meeting and published in local newspaper at least twenty-five days before the meeting (Art. 133).

As a result of the above requirements imposed by the Companies Act, the demand for accounting services increased. This of course led to an increase in the number of accounting firms to provide such services. In his empirical survey, Shinawi (1970, p.53) found that, by 1968, there were twenty accounting firms and the accountants who had been licensed to practice accounting in Saudi Arabia represented six countries: Britain, Egypt, Lebanon, Sudan, United States of America as well as Saudi Arabia. The academic qualifications held by the staff of these firms ranged from a diploma to Ph.D. As to professional titles, one was a C.P.A., five were F.C.A.'s, one was F.A.C.C.A., and seven were Chartered Accountants of Egypt.

Yet there was no law or regulation dealing specifically with the accounting profession in Saudi Arabia except the few rules and articles found in the Companies Act and some other bylaws. It was difficult for the Ministry of Commerce and Industry, in the absence of such laws and regulations, to control the profession and to evaluate the applications of those who applied for a licence. The Ministry realized the seriousness of the problems facing the profession at that time and, as an immediate solution, it issued decision number 422 dated 1968, which specified certain requirements for those who applied for a licence to practice as members of the accounting profession. The requirements, briefly, are (Shinawi, 1970, pp.57-58):

- 1) **Citizenship:** The applicant must be a Saudi or non-Saudi Arab licensed to practise in his native country. The Minister of Commerce and Industry has the authority to license non-Arabs to practice accounting and auditing when he deems it necessary and desirable.
- 2) **Residence:** The applicant must be a resident of Saudi Arabia.
- 3) **Education and Experience:** (a) The applicant should have a doctoral degree in accounting or master's degree in accounting, and one year of training in a licensed accountant's office, or one year of accounting experience in government, a company or a business; (b) or, the applicant should have a bachelor's degree in business or its equivalent and three years training in licensed accountant's office. However, five years accounting experience in government, or company, or a business is considered the equivalent to three years training in a licensed accountant's office. The accounting experience should be gained after graduation in order to be considered.
- 4) **Character:** The applicant should be of good moral character.
- 5) A Licensed accountant is allowed to prepare corporate financial statements only after he has practised accounting or auditing on his own as a public accountant for not less than three years.

The above ministerial order remained in effect till 1974, when the first law of certified accountants was enacted by Royal Decree number 43.

5.3.2 Accounting Practice Under The 1974 Law of Certified Accountants²

In order to keep pace with economic change, there was general agreement on the need to improve the structure of accounting practice and the rules controlling it. This was reflected in 1974, when the

² This section is based on the Law of Certified Accountants which enacted by Royal Decree No. 43 dated 13/7/1394 H. (1974) upon Resolution No. 1008 passed by the Council of Ministers on 9/7/1394 H. (1974). Published in the Official Gazette issue no 2544 of 18/9/1394 H. (1974).

government of Saudi Arabia introduced the "Law of Certified Accountants" by Royal Decree No. 43. This law, which is still in effect with very little amendment, was the first law to regulate the accounting profession. The following sections explain the main features of the Law.

5.3.3.1 Entry Requirements

Article 1 requires that any person wanting to engage in practice as a Public or Chartered Accountant shall register his name in the *ad hoc* register kept by the Ministry of Commerce. The register consists of the following lists:

- a) a list for the registration of Articled Clerks;
- b) a list for the registration of Public Accountants;
- c) a list for the registration of Chartered Accountants.

However, since 1979, registration in the first list (i.e Articled Clerk) is no longer required. As for the remaining two lists, the Law did not go far enough in distinguishing between "Public Accountants" and "Chartered Accountants", except in terms of the type and size of the organisation dealt with by the two categories. For example, Article 17 indicates that:

"Every person who has been entered on the List of Public Accountants may open an office in his own name and practice accounting and auditing of individual enterprises and partnerships whose capital is not in excess of five hundred thousands Riyals".

However, Article 18 indicates that:

"A person whose name is entered on the List of Chartered Accountants shall audit the accounts of individuals, companies, partnerships, banks, public institutions, cooperative societies and others ..."

Due to the significant role of statutory accountants in providing independent opinions on the financial condition of business enterprises, certain restrictions on entry into the profession have been imposed. Only competent and trusted individuals are admitted to the profession in practically all countries. Accordingly, Article 2 sets out the conditions required for entry on to the Register. These conditions are as follows:

- 1) He should be a Saudi National;
- 2) He should be at least 21 years of age;
- 3) He should be fully competent;
- 4) He should be of good behaviour and conduct, and be neither the subject of any legal impediment nor have the subject of a fine or disciplinary order for conduct prejudicial to honesty, honour or morality;
- 5) He should have at least a B.A. degree in accounting, business management or degree in accounting and business administration or any other comparable certificate acknowledged by the Ministry of Education;
- 6) He should have joined a certified accountant's office duly authorized to practice in the Kingdom as a full-time trainee; such fact shall be established by a duly executed contract, a certified copy of which shall be attached to the application for registration.

Article 3 deals with the experience required in addition to the above conditions. This varies according to the qualifications of the applicant as follows:

- a) three years for a person holding a B.A. degree in Accounting and Business Administration or a B.A. Accounting degree;
- b) three years for a person holding a Bachelor of Business Administration degree with a Diploma in Accounting or Taxation ;
- c) four years for a person with a Bachelor of Business Administration degree.

Since no examination is required, it is assumed that any holder of a B.A. degree, either in accounting or in business, who has adequate experience, is competent to enter the list of Public Accountants. However, this is not the case for registration as a Chartered Accountant, where the applicant is required to pass successfully an examination set by the "Higher Committee of Chartered Accountants" (Art.5).

Furthermore, according to Royal Decree No. M/61 which was issued in 1976, entry to the Register of Chartered Accountants is granted to every member of a duly acknowledged international society of Chartered Accountants, if he applies for the same and satisfies the requirements of paragraphs 2 to 6 of Article 2 referred to above (Ibid. para 3). This, of course, gives an opportunity for those who already holding the title of "Chartered Accountant", particularly in the UK and USA, to apply for a licence to practice as an accountant in Saudi Arabia.

5.3.3.2 Registration Procedures and Fees

Articles 8 and 9 respectively deal with the procedures and fees required for registration in the above Lists. Article 8 provides that applications for

registration in any of the Lists referred to in Article 1 shall be submitted to the professional department of the Ministry of Commerce, giving the following particulars:

- 1) the name, surname, nationality, age and place of residence of the applicant for registration;
- 2) a statement showing his educational qualifications, the date on which he obtained them and the authority granting them;
- 3) a statement giving the period of articles and the office concerned;
- 4) a person who has previously obtained a provisional licence to practice accountancy must also attach to his application the following:
 - (a) a certified copy of the provisional licence;
 - (b) a statement giving the period of practice in the profession;
 - (c) a certificate from the Higher Committee of Chartered Accountants testifying to his competency to be registered on the List of Chartered Accountants.

The registration fees also vary according to the type of the List mentioned above. They are 300 hundred Saudi Riyals (SR) for registration in the List of Public Accountants and 500 SR for registration in the List of Chartered Accountants. These fees are not refundable in case of the application being rejected (Art. 9).

With regard to the issue of licences, Article 12 stipulates that a Chartered or Public Accountant shall, after meeting all the qualifications and requirements mentioned above, including the undertaking, be granted a certificate stating that he has been registered on the relevant List, giving the date and number of entry in accordance with such proforma as issued by the Ministry

of Commerce. The certificate granted should be placed in a conspicuous position in his office.

5.3.3.3 Higher Committee Of Chartered Accountants

Articles 14 to 16 deal with the establishment of a committee to be called "The Higher Committee of Chartered Accountants", which consists of the following (Art.14):

- 1) a member of the teaching staff of the accounting department of any Saudi university, whose position is not lower than that of assistant professor, and who shall be selected by the director of the university to which he belongs;
- 2) a chartered accountant practising in the Kingdom, who shall be selected by an order of the Minister of Commerce;
- 3) an expert accountant from the Ministry of Commerce, to be selected by the Minister;
- 4) an expert accountant of the Public Control Registry, to be selected by the Head thereof.

One of the above members should be selected to act as the Committee's Chairman for a period not exceeding three years (Ibid). Membership of the Committee is for three years, and renewable for one term only (Art.15). The primary objective of the Committee is to monitor the overall development of the accounting profession in the Kingdom (Art.16).

However, the Committee is far from accomplishing its basic objectives. Ba-Eissa (1984, p. 310), for example, states:

"In practice, the committee has been ineffective. Apart from preparing a list of the duly recognized international societies of chartered accountants and reviewing the applications of those who practised public

accountancy prior to the introduction of the 1974 Law, none of the committee's proposals and suggestions regarding the amendments to the 1974 Law and development of the accountancy profession has been implemented. The Committee has been meeting twice a year, and its administration and financial facilities have been very poor".

5.3.3.4 Professional Ethics

One of the distinguishing features of any profession is the existence of professional ethics for its members. In the case of the accounting profession, ethics constitute a system of moral principles and the observance of prescribed rules which govern the actions of a professional accountant in his operations, and in his relations with clients, the public and with other accountants. Such rules are usually established by a professional body, such as ICAEW in the UK and AICPA in the USA.

However, so far there is no formal code of ethics concerning accounting practice in Saudi Arabia. In spite of this, some rules similar to those in the United State do exist to a very limited extent. These rules are scattered over the 1974 Law of Certified Accountants and the Companies Act 1965. For example, Articles 11 and 21 of the 1974 Law respectively provide the following statements:

"Chartered and Public Accountants shall, before commencing business, undertake to execute their assignments with integrity, honesty and impartiality and shall observe professional confidentiality" (Art. 11).

"A Chartered and Public Accountant may not engage in any commercial activities or in any work which is inconsistent with or degrading to the profession; he may not acquire business for his profession through advertisements or by any other manner which may be deemed degrading to the profession" (Art. 21).

Article 133 of the Companies Act states that the auditor shall not, otherwise than at the General Meeting, disclose to the shareholders or any other persons, information to which he had access during his audit. If he does, he shall be replaced and held liable for damage.

In practice, compliance by some Saudi accountants with professional ethics in general, and specifically the regulation mentioned above, is questionable. Indeed, a number of Chartered Accountants have expressed their feeling about the absence of a formal code of ethics and considered this issue to be one of the serious problems facing the accounting profession in Saudi Arabia. Al-Kharashi, for example, speaking from his own experience as a chartered accountant, ranks the absence of professional ethics as the foremost problem facing the profession in Saudi Arabia. In answering a question put to him by the economic editor of Al-Yamamah (See Issue No. 1072, September 1989, p.49) concerning the major problems facing the accounting profession in Saudi Arabia, he cited the following:

1. There is no binding code of professional ethics;
2. As a result of the absence of such a code the profession faces the following:

(a) lack of independence of the external auditor with regard to some of his clients. Thus, he works to satisfy the client needs in order to get his contract renewed.

(b) variation in the estimation of auditing fees from one office to another. For example, an accountant who practises for the purpose of obtaining good returns together with honorable work might charge fees of SR 100, while another who offers poor services cheaply might charge only SR 10 for the same transaction;

businessmen want services provided cheaply, and this of course affects the status of the profession and those who deal with it.

3. It is too easy for Saudis who wish to practise accounting and auditing, to obtain a licence. Thus they do not acquire enough experience, which in turn weakens the level of services rendered.

Mr Al-Kharashi went even further by suggesting that the absence of professional ethics has caused some accountants to leave the professional market in recent years in Saudi Arabia. He stressed the necessity to establish a code of professional ethics to be observed by all accountants practising in Saudi Arabia, to increase public awareness of the profession and to establish a specialized accounting institute to produce good quality auditors (Ibid).

5.3.2.5 The Independence and Responsibility of the Auditor

The concept of independence has long been vital to a successful audit practice. When expressing an opinion on the financial statements of a client, the judgement of the auditor must not only be impartial and unbiased, but it must also appear to be so to any outside observer. With the object of maintaining the auditor's independence, Article 22 of the 1974 Law prohibited the auditor from being:

- 1) a partner or director of a company which is being audited by him nor shall he undertake any administrative duties for it;
- 2) a partner or employee of the persons mentioned in the preceding paragraph;
- 3) a relation down to the fourth degree of any person who is in charge of the company's management or accounts.

As far as the responsibility of the auditor is concerned, Article 24 of the 1974 Law provides that a Chartered or Public accountant shall be liable for damages suffered by a client or other third parties as a result of errors committed by him in the course of his duties. When such errors are the responsibility of more than one Chartered or Public accountant, they shall be jointly liable (Ibid).

5.3.3.6 The Audit Report

The audit report constitutes the end product of an audit of a business enterprise expressing the auditor's opinion on the client's financial statements. The audit report is usually addressed to those who retained the auditors, i.e the board of directors in the case of

corporations. Most of the countries which have an organised accounting body have adopted an agreed form of audit report.

In Saudi Arabia, however, there is no mandatory standard form of the audit report. Accordingly, the style and wording vary considerably and are widely affected by the background of the auditor and the prevailing law and circumstances. Evidence of such can be clearly seen through the following two audit reports which were published recently in the local newspapers by two different accounting firms.³

Example I: AUDITOR'S REPORT

To the Shareholders of Saudi Public Transport Co.

"We have examined the final accounts of the Saudi Public Transport Company - Saudi Joint Stock Company - set out in pages 2 to 16. Our examination included such tests of the accounting records and other auditing procedures as we considered necessary.

In our opinion the final accounts present fairly the financial position of the Company as at 29/6/1409 H. [1989] and the result of its operations, and sources and application of funds for the year then ended."

For Whinney Murray & Co.
Atta H. Al-Beyok, Statuary Accountant
Licence No. (7)

Source: Okaz (daily newspaper), Issue No. 8686, dated April 30, 1990, p. 21 (in Arabic and translated by the author).

³ These two audit reports were selected at random and used in this study for the purpose of analysis and comparison between the two forms and not for any other purpose whatsoever.

Example II: AUDITOR'S REPORT

To the Shareholders of National Industrial Co.

Saudi Joint Stock Company
Riyadh - Saudi Arabia

"We have examined the general balance sheet of National Industrial Company as at 31/12/1989, profit and loss account for the period from 1/1/1989 to 31/12/1989, as well as the statement of sources and application of funds for the same period. Our examination was made in accordance with generally accepted auditing standards; and accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary. We have obtained the information and explanation which we considered necessary for the purpose of our audit.

In our opinion .. National Industrial Company, Saudi Joint Stock Company, keeps organised accounting books and records. The balance sheet and its notes from No. (1) to No. (18), the profit and loss account, as well as the statement of sources and application of funds present fairly the financial position of the company as at 31/12/1989 and the result of its operations for the same period in accordance with the principles and accounting polices followed by the company, other known accounting bases, and in accordance with company's bylaws as well as the Companies Code."

Date: 1/4/1990
Saudi Accountants Office
Partner: Ibrahim AL-Sabeal
Licence No. (76)

Source: Okaz (daily newspaper), Issue No. 8698, dated May 12, 1990, p. 17 (in Arabic and translated by the author).

The above two forms of audit reports suggest the following observations:

- 1) Both reports are directed to the shareholders of the company.
- 2) Although both reports consist of two main paragraphs, the first report is shorter than the second.
- 3) The first report contains only a general description of the work performed. For example, it does not refer to any generally accepted auditing standards on which the report is based, nor does it mention whether the final accounts were prepared in accordance with the Companies Code and company's bylaws.
- 4) In contrast, the second report does refer to generally accepted auditing standards as well as the Companies Code. However, it fails to specify whose auditing standards are applied.
- 5) The date is missing in the first report, despite its importance to the users of the report.

Given the fact that as yet no specific form of audit report is binding on all accountants in Saudi Arabia, the variation between the two reports is attributable to the experience and background of the auditors.

5.3.3.7 Violations and Trial Proceedings

Articles 25 to 29 of the 1974 Law deal with violation and trial proceedings. For example, to protect the public interest, Article 25 emphasizes that any

person who falsely assumes the title "Chartered or Public Accountant" or any similar term, or who submits false documents in order to have himself registered on any of the Lists referred to earlier shall be punished with imprisonment for not more than two years and/or a fine not exceeding ten thousands Riyals. Moreover, the penalty also extends to the deletion of the defaulter's name if already registered, the closure of his office, and the publication of the judgement concerning this matter in the official Gazette and a widely circulated newspaper (Ibid).

In conclusion, then, the law specifies the qualifications and requirements needed to enter the profession as a registered accountant. It restricts the practice of auditing to those who have some academic qualification as well as previous experience. However, the 1974 Law does not go far enough, particularly concerning the accounting and auditing principles to be used, as well as the professional ethics.

5.3.3 Recent Developments

With rapid economic and industrial development in Saudi Arabia during the past decade, huge numbers of corporations, limited liability companies and other business entities have been formed (see chapter 6) As a result, the demand for public accountants' services has increased.

In recent years, the Ministry of Commerce has found that the financial statements prepared by the accountants

in these business organisations were non-comparable and inadequate due to the application of diverse accounting principles. Meanwhile, there were no uniform auditing standards to be followed. This made it difficult for external auditors to give an opinion regarding the financial position of enterprises, and audit reports varied widely, as shown by the examples given earlier.

Since the government is aware of this problem and its possible negative effect on economic development, the Ministry of Commerce has agreed to finance a project to study and develop the accounting profession in Saudi Arabia. The project has been divided into three stages. Stage one was a comparative study of three countries to benefit from their experience. Stage two was concerned with the development of national accounting and auditing standards. The results of these two stages were published in two volumes. The first one is entitled "Auditing Standards" and the second is entitled "Accounting Concepts and Objectives". The third stage concerns the development of other aspects of the profession such as the introduction of a code of professional ethics, but the output of this stage has not yet been published.

In general this phase is considered as the starting point toward the advancement of the accounting profession in Saudi Arabia. Its distinguishing feature is the move to regulate the accounting profession by introducing

accounting and auditing standards for financial reporting.⁴

5.4 The Main Features of the New Proposed Law of Certified Accountants

In 1981, the Ministry of Commerce drafted a new proposed law, which was revised several times in the following years and has still not been enacted. In a recent interview with the Chairman of the "Higher Committee of Chartered Accountants" (interview No. 15), he mentioned that the draft of the new proposed law has been sent to the Council of Ministers for further study and approval. To the best of the researcher's knowledge, the new proposed law has not yet been approved. Perhaps this delay may be attributable to the desire of the Ministry of Commerce to refer in the new law to the accounting and auditing standards, which were recently published as the output of the second stage of the comprehensive project undertaken by the Ministry to develop the accounting profession.⁵

However, during the course of the above interview the researcher had the opportunity to examine the draft of the new proposed law, which includes two notable features:

Firstly, the new law calls for the establishment of a new Board to be called "Saudi Board of Certified Public Accountants (SBCPA)" which would function for the overall

⁴ The approach adopted and the contents of these two volumes will be reviewed and evaluated in chapter 9.

⁵ While this thesis in the process of submission, the author learned that the new law was actually enacted by Royal Decree No. M/12 dated 13/5/1412 (1992).

development of the accounting profession in general and the following aspects in particular:

- 1) Preparing accounting and auditing standards to be followed by public accountants practising the accounting profession in Saudi Arabia;
- 2) Organising the continuing education programmes and professional examinations required for a licence to practice accounting profession;
- 3) Carrying out research and studies concerning the development of accounting and auditing;
- 4) Publishing books, periodicals, and bulletins on accounting subjects;
- 5) Suggesting any amendments which need to be made to the accounting laws and regulations;
- 6) Participating in local and international symposia concerning the development of the accounting profession.

The above body would be administered by a Board of Directors consisting of thirteen members as follows:

- 1) The Minister of Commerce (President);
- 2) The Deputy Minister of Commerce (Vice President);
- 3) The Deputy Minister of Finance and National Economy for financial affairs and accounts (member);
- 4) The Vice President of the General Audit Bureau (member);
- 5) Two Saudi academicians from accounting departments in one or more Saudi Universities to be elected according to agreement between the Ministers of Commerce and Higher Education;
- 6) A representative from the Council of the Chamber of Commerce and Industry to be appointed by the Minister of Commerce upon the recommendation of the Council; and
- 7) Six members from the public accountants to be elected in General Meeting of the Board for three years, renewable for one term only. However, in an exceptional case, they will be appointed to

the Board of Directors for the first time for five years by order of the Minister of Commerce.

Secondly, the proposed law calls for the establishment of the "Saudi Institute of Certified Accountants (SICPA)". The function of SICPA would be similar to that of ICAEW in the UK and AICPA in the USA. Moreover, according to the proposed law, entry to the profession would be limited to Saudis who hold accounting or business degrees and are members of SICPA. However, in order to become a member of SICPA, a candidate would be required to attend formal seminars and pass a professional examination to be prepared by the SBCPA.

Although professional authority under the new proposal will continue to be fully exercised by the Ministry of Commerce, there is no doubt that the establishment of the above two bodies will enhance the development of accounting in Saudi Arabia.

5.5 Factors Affecting the Development of Accounting Practice in Saudi Arabia

The development of accounting in Saudi Arabia, as in many developing countries, has been affected by a number of factors, of which the following are perhaps the most important:

1. Type of Business Ownership;
2. Foreign influence through accounting firms, companies, and education;
3. Rapid economic development;
4. Government laws and regulations;
5. Saudi Accounting Association (SAA).

5.5.1 Type of Business Ownership

The type of ownership helps in shaping the principles and practice of accounting in many countries (Nobes and Parker, 1985). Individual proprietorships and small family groups are the dominant features of ownership in many developing countries, and Saudi Arabia is no exception. According to a recent report, the total number of individual proprietorships and firms registered throughout the Kingdom reached 297,316 by the end of 1987. Table 5.1 shows the breakdown of individual proprietorships and firms registered for the period from 1985-87, by province.

Table 5.1
Individual Proprietorships and Firms Registered
in Saudi Arabia up to the end of 1987

Province	1985	1986	1987	Cumulative Total
Central	7,141	4,573	4,690	100,187
Western	10,265	2,545	6,064	106,499
Southern	1,703	4,276	1,223	18,910
Eastern	3,036	4,187	552	52,063
Northern	1,505	964	1,050	19,657
Total	23,650	16,545	13,579	297,316

Source: Ministry of Commerce (published in Saudi Arabia Monetary Agency's Annual Report, 1988, p. 107).

The disclosure of financial information in such small individually-owned businesses is minimal, because usually these individuals tend to resort to secrecy and

protection of information from competitors, government and the public.

5.5.2 Foreign influence

The foreign influence on accounting practice in Saudi Arabia operates through three different channels: foreign accounting firms, foreign companies, and foreign accounting education.

5.5.2.1 Foreign accounting firms

As stated earlier, the first accounting firm licensed to practise public accounting in Saudi Arabia was a foreign firm. It was also mentioned that by the end of 1968, there were twenty accounting firms in operation, representing six countries including Saudi Arabia. These foreign accounting firms have certain negative impact upon the local accounting system. As Enthoven (1991, p.271) has observed:

"In many [developing] countries, foreign accounting firms operate. They tend to follow foreign accounting/auditing pronouncements, which may not help develop useful local standards. In general, accounting firms are not involved adequately in social and economic programmes; nor do they assist sufficiently in fulfilling the accounting needs of smaller firms either directly or through development institutions."

Indeed, the foreign firms still constitute a significant proportion of the total accounting firms operating in Saudi Arabia. As at the end of 1405 (1985), 49 (31%) of the total Accountants and Auditors offices licensed to practise accounting in Saudi Arabia were non-

Saudi (SAMA's Annual Report, 1986, p.113). In addition, the "Big 8" firms were also represented in Saudi Arabia, either in the form of branches of their UK or USA offices, or by establishing an association relationship with an operating firm in Saudi Arabia.

5.5.2.2 Foreign Companies.

Foreign companies are one of the main vehicles for the transfer of accounting ideas and procedures from one country to another. This is not a new phenomenon; in the sixteenth century, for example, double-entry book-keeping and other accounting procedures were introduced to England and other European countries as a result of trade with Italian companies (Lee, 1975, p.9).

As for Saudi Arabia, with rapid economic development during the past two decades, many foreign companies, particularly from the United States, United Kingdom, and other Western countries, have played a significant part in constructing the main infrastructure such as roads, dams and schools. For example, in 1982, only 37 percent of the total value of development contracts was awarded to Saudi contractors compared with their foreign counterparts (Statistical Summary, 1983, p.44). Although the Saudi contractors succeeded in increasing their share of government project contracts by 18 percent over the Fourth Plan period (1985-90) due to the enforcement of the thirty percent rule which states that "at least 30 percent of the constructions value of government

contracts must be awarded to Saudi constructions firms", the foreign contractors remain substantial.

There are positive as well as negative effects of these foreign companies upon the local accounting system. The positive effect stems from the fact that their Saudi staff are introduced to modern accounting practices such as the use of computer technology in day-to-day business operations. Indeed, some of the new Saudi graduates who have joined these foreign companies have already had an opportunity to go abroad for further study and training in various accounting fields.⁶

As far as the negative effect is concerned, most of these foreign companies use the accounting principles applied in their mother countries, which might not be relevant to the local needs, due to the differences between the two environments.

5.5.2.3 Foreign Influence Through Education

As in the case of most developing countries, the government of Saudi Arabia has sent many students abroad, particularly to the United States and Great Britain, to gain knowledge and experience in various educational fields, including accounting and business. In 1403/04 H. (1983/84), the number of male and female students studying on scholarships abroad was 10,092 (SAMA Annual Report, 1986, p.127). Further, Abdeen and Yavas (1985, p.162) state:

⁶ Foreign companies operating in Saudi Arabia were encouraged to employ more Saudi nationals in line with the recent Government policy to reduce foreign manpower in the country.

"The majority of Saudi faculty with doctorates employed by KSU and KAU were trained in the United States. Similarly, the non-Saudi faculty at UPM and KSU received their degrees from North American universities. The non-Saudi faculty at KAU, on the other hand, were educated in Europe (England and France), Egypt, and the United States."

The influence of foreign education on accounting in Saudi Arabia stems from the fact that "the diversity in the backgrounds of accounting faculty contributes to the teaching of a variety of courses in accounting principles, as well as auditing standards and procedures. The accounting systems, methods, and techniques taught are oriented toward the accounting environment of the country in which the degree is obtained" (Ibid).

5.5.3 Rapid Economic Development

There is a close relationship between the level of economic development in a given country and the stage of accounting development and practice in the same country. This idea is well articulated by Arpan and Radebaugh (1985, p.20), who argue:

"At extremely low levels of economic development, there is little economic activity and correspondingly little financial, tax, or managerial accounting. As the level of economic activity and the size of companies increase, there is a corresponding increase in accounting activity ..."

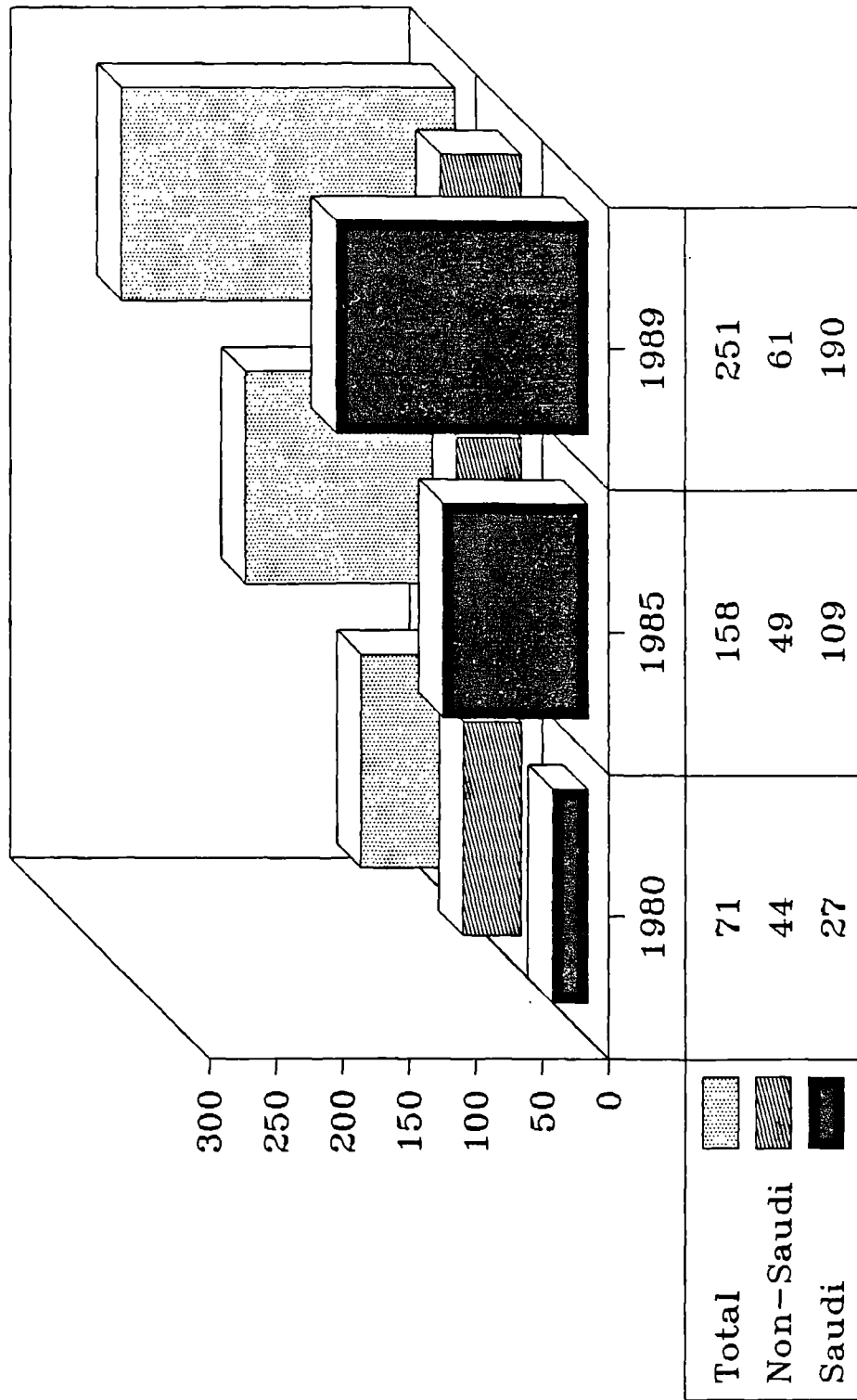
The rapid growth of the Saudi Arabian economy explained earlier (see chapter 3) has had a great influence upon the accounting profession. Consumption has increased rapidly due to the rise in per capita income

from oil revenues. Exports and imports have increased. Comprehensive development plans covering all economic sectors have been undertaken and huge amounts of money are being allocated. As a result of this huge investment there has been a remarkable development in the forms of business enterprises over the last twenty years. This trend has been in the direction of establishing partnerships and corporations instead of individual or family-owned firms. The significant growth in the number of corporations since the early 1970s has demanded a wide range of accounting services. Thus, the number of accounting firms which provide such services has increased rapidly.

Figure 5.1 shows the number of licensed accountants in Saudi Arabia during the past decade. The total number of licensed accountants was 71 in 1980, of which only 27 (38 percent) were Saudi. However, during the following five years (1980 - 1985) the number of Saudi licensed accountants increased rapidly, reaching one hundred and nine by the end of 1985; meanwhile, the total number of non-Saudi accountants increased by only five.

This relatively large growth in the number of Saudi licensed accountants is attributable to the change in the requirements in the early 1980s, when the new applicant was no longer required to have had two years of practical experience with a public accounting firm as laid down previously in article 2 of the 1974 Law of Certified Accountants.

Figure 5.1
Public Accountants Licensed
in Saudi Arabia as at the end of 1989



Source: Compiled From a Guide for Professionals, Ministry of Trade, 1989.

Furthermore, by the end of 1989, the total number of licensed accountants jumped to 251, of which 190 were Saudi nationals.

5.5.4 Government Laws and Regulations

The government of Saudi Arabia has enacted a number of laws and regulations in response to the changing needs of society. Examples of such laws related to accounting, are Income Tax and Zakat Law, Companies Law, the Law of Certified Accountants, and Foreign Investment Law.

An effect of these laws on accounting development, is that they provide some basic guidelines for auditors, together with other regulations to improve the reliability of accounting information. For example, the Companies Act (Art.130) required that at annual general meeting, the shareholders appoint the auditor(s) from among those who practise accounting in Saudi Arabia. Articles (136-142) specified the responsibilities and the rights of the auditor in examining the company's books and records. Furthermore, the Income Tax and Zakat Regulations required all companies to submit their final financial statements to the Zakat Income Tax Department after being attested by a statutory accountant. Although these laws have positively affected the development of accounting in Saudi Arabia, they are still general in nature and lack specificity.

5.5.5 Saudi Accounting Association

So far there is no professional accounting body in Saudi Arabia comparable to ICAEW in the United Kingdom and AICPA in the United States. Ba-Eissa (1984, pp.306-307) suggested two reasons for this:

1. The 1974 Law of Certified Accountants does not make any provision for the establishment of a professional body;

2. There has been no attempt to form such a body because: (a) most of the foreigners who dominated accounting practice in Saudi Arabia until the beginning of the 1980s cared little about the organisation of accounting in a country that was not theirs, and (b) the formation of a professional body might be regarded as a political activity that is not acceptable under the present political system in the country.

Nevertheless, this attitude seems to have changed in recent years. The establishment of the Saudi Accounting Association (SAA) could be viewed as an example of such a change. The SAA was set up in 1980 by some members of the accounting department at King Saudi University with the following objectives (Ba-Eissa, 1984, P.308):

- 1) To develop accounting thought in Saudi Arabia.
- 2) To encourage the contribution of professional accountants to the development of accounting thought in Saudi Arabia.
- 3) To facilitate the exchange of ideas between the Association and those other organisations concerned with accounting in Saudi Arabia as well as in other parts of the world.

- 4) To provide advice and necessary research for the purpose of developing the profession of accounting.

The membership of SAA is divided into three categories as follows (SAA's Bylaws, pp.4-5):

A) **Honorary members:** persons who have provided extraordinary services to the Association either in money or in kind, or participated in Association activities both within and outside the Kingdom. Honorary members are selected by order of the general meeting upon the recommendation of the Board of Directors. This type of membership is exempt from registration and annual subscription fees.

b) **Active members:** who should hold a university degree in an appropriate specialization (i.e. accounting or business with an emphasis in accounting), be resident in the Kingdom of Saudi Arabia, and satisfy the conditions and procedures set out in article 5 of the Association's Bylaws.

c) **Associate members:** those who are not resident in the Kingdom of Saudi Arabia but wish to become members of the SAA.

The SAA is administered by a Board of Directors consisting of not more than nine members, who are elected by the General Assembly from among the active members (Bylaws, Art. 8). The members should select one of their number to act as Chairman and another as Vice-chairman. The term of office of the chairman and his deputy is two years, renewable for one further term only (Ibid.).

As for the impact of the SAA on the development of accounting in Saudi Arabia, since its inception it has held several conferences. Although the idea of such conferences is useful as far as the development of accounting is concerned, efforts so far mainly confined to the development of the accounting profession by means of establishing accounting and auditing standards for external financial reporting in Saudi Arabia. For example, 5 out of 7 researches and 3 out of 5 discussion papers presented in the first accounting conference in Saudi Arabia held in 1981, were devoted to the accounting profession and auditing standards. The subsequent conferences held in 1983, 1987 and 1989 show similar emphasis. In contrast, little attention has been paid to the development of accounting in the public sector, or to accounting education and training.

Indeed, the function of SAA is hampered by the other commitments of its members which inhibit their participation in its activities. In fact, one factor which might affect the SAA's function is that the majority of its members are academic staff who are engaged in full-time teaching for most of the year and are accordingly unable to participate fully in the SAA's activities, particularly those which take place during the academic year. Other members of the profession seem to lack enthusiasm for participating in these activities because they consider the SAA to be an academic

association and would prefer to establish their own professional association.⁷

5.6 The Status of Accounting Practice in Saudi Arabia: Results of the Empirical Survey

5.6.1 Objectives and Approach

The purpose of this empirical survey was to contribute to better understanding of some practical aspects of current accounting practice in Saudi Arabia. Matters investigated include, among other things, the type of accounting standards widely referred to by accountants, the relevance of such standards to the Saudi socio-economic environment, reasons for diversity in accounting practice, and types of accounting services rendered.

Furthermore, given the public dissatisfaction with the published financial statements of Saudi corporations which was highlighted recently by the local press (see chapter 6), the study seeks the opinion of public accountants who work as external auditors for such enterprises, about the major accounting problems which might be detrimental to their published financial statements.

Finally, the survey also aims to seek public accountants' opinions regarding the recent accounting developments in Saudi Arabia, e.g. to what extent were local accountants actually involved in the establishment of the accounting and auditing guidelines produced so

⁷ Based on an interview with the SAA's Secretary, KSU, Riyadh, December, 1989.

far? Why have these guidelines not become mandatory, so long after their publication? and does the current status of the accounting profession in Saudi Arabia, particularly in the absence of a professional body, encourage further developments in this direction, including establishing more accounting standards for external financial reporting?

5.6.1.1 The Questionnaire Design

The public accountants' questionnaire (see Appendix A) was designed to collect data regarding the above issues. The Questionnaire was short and more specific. It consisted of three parts: (1) General Data; (2) Status of Accounting Practices; and (3) the Recent Accounting Guidelines in Saudi Arabia (see table 5.2).⁸

Table 5.2
The Structure of the Accountants' Questionnaire

Part No.	Title	No. of Qs.	Sequence
1	General Data	10	1-10
2	Status of Accounting Practices	8	11-18
3	Recent Accounting Guidelines	10	19-28

The questionnaire was accompanied by a covering letter explaining the main purpose of the study and setting forth guidelines for its completion. In addition, a letter from the Dean of the Faculty of Economics and Administration was enclosed to introduce the researcher

⁸ Copy of the questionnaire is reproduced in appendix A.

to the participants and to encourage them to cooperate with the study.

5.6.1.2 The Survey Sample

According to a Ministry of Commerce official, the number of accountants licensed to practice accounting services throughout the Kingdom of Saudi Arabia totalled 251 in December of 1989 (see figure 5.1 above). Given the huge distance which separate the Kingdom's five regions from each other and due to practical considerations such as time, finance, and facility requirements, it was impossible for the researcher to survey all licensed accountants in Saudi Arabia.

It was decided that a sample of 100 licensed accountants would be sufficient. The sample was divided equally between the two main regions of Saudi Arabia, the central and western. These two regions were selected in preference to the others because they are the most populated. For example, the former contains Riyadh, the capital city of Saudi Arabia; while the latter contains Jeddah, the commercial centre and the main port of the Kingdom on the Red Sea. In addition, Jeddah is the location of the researcher's employer (King Abdul Aziz University) which of course facilitated contact with the accountants in that area.

5.6.1.3 Distribution Procedures

The distribution of the questionnaire was undertaken as follows: the first portion (50) of the sample which represented the central region (Riyadh and the

surrounding areas) received a copy of the questionnaire during the SAA meeting which was held on the 5th of December 1989 at the Riyadh Chamber of Commerce and Industry (RCCI). The distribution was made after obtaining advance permission from the presidents of the SAA and RCCI. With the help of the SAA members, the researcher was able to collect 30 questionnaires from this portion of the sample immediately after the end of the meeting, while 15 arrived later by post.

The second portion (50) of the sample which represented the western region (Jeddah area) either received copies of the questionnaire by post or had them delivered personally by the researcher during afternoon working hours. A list of licensed accountants practising in the Jeddah area was obtained from the secretary of the accounting department at King Abdul Aziz University.

Table 5.3 shows the distribution of the questionnaire and the responses to the survey received from the two regions.

Table 5.3
Number of Questionnaires Delivered and
Responses to the Survey

Region	Number of Questionnaires Delivered	Number of Responses	Percentage
Central (Riyadh)	50	45	90
Western (Jeddah)	50	41	82
	-----	-----	-----
Total	100	86	86
	====	====	====

5.5.2 Analysis of the Responses

This section is divided into five sub-sections: background information, accounting standards in practice, respondents' views of the major problems facing Saudi corporations, types of services rendered and respondents' views of the recent accounting guidelines. This classification is based on the construction of the questionnaire explained earlier.

5.5.2.1 Background Information

The first part of the questionnaire sought some basic data concerning the respondent: his position in the firm, education, work experience, place of education and experience, and whether he is a member of any accounting society. Such preliminary data were considered necessary, as the respondent's background may have some effect on his answers. Moreover, starting by simple questions usually encourages respondents to proceed to the main questions of the survey.

At the outset, respondents were asked to specify their position in the firm in which they are employed. Although the questionnaire was not directed to specific positions in the firm, the responses received show that the majority of the respondents (42%) were owners, next were partners (28%) and accountants in charge (23%) while the remaining (7%) did not report their position.

In questions 2 to 9, respondents were asked to provide some statistical data concerning their qualifications and experience, as well as to indicate the

place in which these were obtained. Responses to these questions are tabulated and discussed below.

Table 5.4 Basic Data on Respondents

Education Level	%	Place of Education	%
a. B.A. Accounting	52	a. Saudi Arabia	73
b. B.A. Business	37	b. Arab Countries	19
c. Master Degree	9	c. Foreign Countries	8
d. Ph.D Degree	2		
Total	--- 100 ===		--- 100 ===
Experience	%	Place of Experience	%
a. Less than 5 Years	13	a. Accounting Firms	47
b. Between 5-10 Years	67	b. Gov. Departments	39
c. More than 10 Years	20	c. Private Businesses	35
		d. Banks	27
Total	--- 100 ===		--- 100* ====

* Total of percentages exceeds 100% because some respondents have work experience in more than one place.

According to table 5.4, more than 50% of the respondents hold a B.A. in accounting, and 73% received their education in Saudi Arabia.

As far as previous experience is concerned, the majority had between 5 and 10 years experience in accounting and 47% gained their experience in accounting firms. Only 17% of the respondents stated that their work involved use of the computer.

It is worth mentioning that although the Accountants Law of 1974 lays down the period of experience required for a licence, which varies according to the type of degree held by the applicant (Art.3), it leaves the decision as to type of experience to the Ministry of Commerce and normally any previous experience which included some accounting and auditing work would be accepted.

Moreover, the Accountants Law does not require an applicant to sit for professional examinations or to have a professional accounting qualification, in order to be granted a licence to practise accounting. However, a number of public accountants in Saudi Arabia have recently argued that a professional qualification from any recognised accounting body should be made a precondition for such a licence.⁹ This survey shows that only nine respondents have a professional qualification from an accounting society in another country. Of these, four respondents have American CPA, three have British ACA, and two have a professional title from Egypt.

In order to evaluate the level of new accounting graduates, the respondents were asked the following questions:

"How do you evaluate the level of the new accounting graduates who apply to practise in your firm as accountants under-training?"

⁹ See for example, an interview with Mr. Al-Rashed, managing director of Al-Rashed Certified Accountants, in a series of interviews conducted by the Economic Editor of Al-Yamamah on the topic of "Statutory Accountants Under Al-Yamamah Microscope", Al-Yamamah, issues No. 1074 and 1075 dated 5th and 11th October, 1989.

In answering this question, respondents were asked to use three possible categories (good, adequate and weak). The answers received show that 56% of the respondents believed that the level of new accounting graduates is adequate, 23% of the respondents believed it is good while 21% of the respondents believed it is weak. This later group pointed out that such weakness embedded mainly in practical side. Indeed, this was not surprising because the current accounting programme does not include real case study material nor does it require the students to spend sometimes in industry as a part of their course (see chapter 4).

5.6.2.2 Accounting Standards in Practice

One of the objectives of the survey was to determine the type of accounting standards widely used by accountants in Saudi Arabia and the reasons why they are used. This is particularly important due the fact that there is no set of national uniform accounting standards in Saudi Arabia. The application of diverse accounting standards is likely to affect the accounting information contained in financial statements (Al-Rehaily, 1989), and any future development of accounting in the country. Thus, questions 11-13 of the questionnaire were designed to reveal information concerning these issues.

Table 5.5
Accounting Standards in Practice

Type of Accounting Standards in Practice	No.	%
a. International Accounting Standards (IASs)	38	44
b. American Accounting Standards	26	30
c. British Accounting Standards	16	19
d. Other (GAAPs)	6	7
Total	86	100

Table 5.5 shows that 38, or 44 percent, of the respondents believed that the International Accounting Standards (IASs) prepared and published by the International Accounting Standards Committee (IASC) are widely used by practitioners in Saudi Arabia. These are followed by American and British Accounting Standards, according to the respondents (30% and 19% respectively). The remaining 7% of the respondents referred to the use of "generally accepted accounting principles", though they failed to specify the origin of the phrase. Given the fact that there is no set of national generally accepted accounting principles in Saudi Arabia, it is most likely that the GAAPs referred to by the respondents are either American or British or IASC's ones.

It should be pointed out, however, that the popularity of IASs is not unique to Saudi Arabia; it is found in many developing countries, particularly in the Middle East. For example, in recent years, IASs were (a) adopted by Oman in 1986 as guidelines to be used by local practitioners, and (b) modified and adopted by both Egypt

in 1980 and Kuwait in 1987 as national accounting standards. Moreover, it could be argued that one of the main reasons for the popularity of the IASs over the other standards in this part of the world might be the availability of their text in the Arabic language, as they were translated and published by Arab Society of Certified Accountants (ASCA) in recent years.

It may be worth noting that the ASCA was established in 1984, and seeks to adapt accounting, financial reporting and audit standards and practices to the needs of Arab economies. Its current Board of Directors include three Saudi members, one academic and two public accountants. In 1989, the ASCA organized the first qualifying examinations of "Arab Certified Accountant".

Nevertheless, a number of accounting scholars have argued against the adoption or modification of IASs by developing countries. Their argument is that IASs are largely a modification of accounting standards in the USA and the UK, which have different socio-economic environments from those of developing countries (see for example, Briston, 1978; Samuel and Oliga, 1982; Perera, 1985; Belkaoui, 1988).

When asked about the reasons behind the spread of foreign accounting standards in Saudi Arabia, 62% of the respondents believed that the absence of local accounting standards is the main factor behind this phenomenon; 28% attributed it to the accountants' education and experience; while 22% believed that the establishment of

branches of foreign accounting firms contributes to the spread of foreign accounting standards, as these branches tend to bring with them staff, ideas and standards from their original countries.

As for the question of relevance of these foreign accounting standards to the local socio-economic environment, 93% of the respondents answered "no" to this question, while the remaining 7% had no clear opinion. None of the respondents believed that foreign accounting standards are relevant to the local socio-economic environment. Of those who said "no", 76% believed that each country has its own socio-economic, political and cultural environment, and thus should develop its own accounting standards.

5.6.2.3 Respondents' View of the Major Problems Facing Saudi Corporations

In recent years, members of the public have expressed their dissatisfaction with the financial statements published by Saudi corporations. They believed that such statements were inadequate for the purpose of decision-making because they were out of date, not well presented and a number of transactions were omitted (see chapter 6). Moreover, recent research revealed that annual reports of some of these enterprises did not include their financial statements (Bahjatt, 1986, p.93).

Detailed study of the accounting systems of Saudi corporations is the subject of the next chapter. The purpose of the rest of this section, however, is to

report the result of a study that sought public accountants' views concerning the major problems facing these enterprises, which might affect their published financial statements. Responses received concerning these inquiries are shown in following table.

Table 5.6
Major Problems facing Saudi Corporations

Problems	No.	%
a. Shortage of accountants	41	48
b. Weakness of internal control system	29	34
c. Application of diverse accounting standards	11	13
d. Combination of a, b and c	5	6
Total	86	100

When asked if the adoption of a uniform accounting system by Saudi corporations would alleviate or at least reduce most of their accounting problems, 73% of respondents answered in the affirmative. 27% of the respondents agreed on the need for uniformity, particularly for those enterprises which have similar business activities, but believed that such a system alone would not be the final solution to the problems currently facing corporations. They argued that the problems differ from one enterprise to another and thus the problems of each one should be dealt with separately.

Assuming that a uniform accounting system was to be adopted by corporations, respondents were asked who should establish such a system, and were furnished with

three alternative possibilities from which to select. Their answers were as follows:

- (1) 47% stated that it should be established by a team including representatives from the accounting profession, accounting academics, and government officials;
- (2) 28% stated that it should be established by a government agency such as the Ministry of Commerce;
- (3) 25% stated that it should be established by a private accounting body.

The author believes that a joint effort by the public accountants, the accounting academics, and representatives of government departments that use accounting information in their operations is needed for formalization of such a system and for any future development of accounting in Saudi Arabia (see chapter 10).

5.6.2.4 Types of Services Rendered

The rapid economic development of Saudi Arabia in recent years has created an increasing demand for accounting services. The 1974 Law of Certified Accountants states the types of firm which each category of registered accountants and auditors and their assistants may audit (Articles 17 and 18). Accordingly, it is presumed that public accountants may render any services which might include book-keeping, auditing, Zakat and tax services, liquidation, management services, system design and installation, and others.

Respondents were asked to indicate the types of accounting service that are most performed by their firms. Table 5.7 shows the responses to this question. This table lists types of accounting services along with the number of responses and their percentage of overall responses. These services are then ranked from 1 to 6, representing the highest to lowest percentage. It is clear from the table that 74% of the respondents considered auditing services the most important activity of their firms, with income tax and Zakat services, and book-keeping the two next most important. The render of other services, however, ranged from 10 to 24 percent of the overall activities of accounting firms. It is interesting to note that management services rank as the lowest activity.

Table 5.7
Type and Rank of Services Rendered by Public
Accountants In Saudi Arabia

Type of Services Rendered	No.	%	Rank
- Auditing	64	74	1
- Income Tax and Zakat	50	58	2
- Solvency and Liquidation	21	24	4
- Management Services	9	10	6
- System Design and Installation	14	16	5
- Book-keeping	37	43	3

Based on the above results, it must be emphasised that public accountants in Saudi Arabia should widen their services to include effectiveness and efficiency

audit, and feasibility studies. Such services are much needed at the present time, because the financial situation of the country now is not as in few years ago. The Kingdom is now in shortage of cash, and the available fund should be allocated more economically. Public accountants should also cooperate with local academic institutions, particularly with regard to the type of training programmes needed for local accountants in order to enhance the level of services rendered.

5.6.2.5 Respondents' Views of the Recent Accounting Guidelines in Saudi Arabia

It has been suggested that the responsibility for issuing accounting standards lies primarily with professionally qualified accountants (Arnold, Hope and Southworth, 1985, p.69). One of the objectives of this empirical survey was to assess the recent accounting and auditing guidelines published in Saudi Arabia from the professional accountants' viewpoint. Since these guidelines are mainly concerned with professional accountants' work, the first enquiry which came to mind was whether they were actually involved in the process of setting these guidelines in the first place.

The study shows that only two local professional accountants had actually participated in the process of setting the accounting and auditing guidelines established so far in Saudi Arabia. Most of the work was undertaken by foreign accounting experts and Saudi accounting academics. However, 75% of the respondents

stated that they had seen the contents of the recent accounting and auditing guidelines published by the Ministry of Commerce.

When asked their opinions concerning the contents of these guidelines, 57% of the respondents perceived them as similar to those of the USA and the UK; 23% of the respondents perceived them as concentrating on external financial reporting and external auditing; while 20% of the respondents perceived them as long and containing unnecessary details.

As for the reasons why these accounting and auditing guidelines have not become mandatory after such a long time (more than four years), respondents were provided with three possible reasons, and invited to suggest reasons of their own. Responses to this enquiry are shown in following table.

Table 5.8
Reasons Contributing to the Delay in Implementing
the Recent Accounting and Auditing Guidelines

Reasons	No.	%
a. Lack of enforcement body	55	64
b. Lack of institutional support	41	48
c. Lack of cooperation from interested parties	16	19
d. Do not know	13	15

According to table 5.8, the lack of an enforcement body and institutional support are the main reasons contributing to the delay in implementing the accounting and auditing guidelines established so far. Other factors

such as lack of cooperation from interested parties (professionals, accountants in industry and the Ministry of Commerce) were believed to be among the reasons which delay the implementation of these guidelines.

It should be pointed out that, since there is as yet no professional accounting body in Saudi Arabia, the task of monitoring the implementation of these guidelines rests in the hands of the Ministry of Commerce, represented by the Companies Department. However, there is still much doubt as to whether the Companies Department is actually able to handle this task, given the fact that it currently suffers from a shortage of staff, both in quantity and quality.¹⁰

In order to clarify this point the author asked Mr Al-Rashed, managing partner of a leading Saudi accounting firm, who was involved in the process of setting the accounting and auditing guidelines, whether the delay was attributable to the lack of technical staff in the Companies Department. Mr. Al-Rashed seems to hold a different view, saying that (*interview No. 11*):

"What you have said about the Companies Department staff is your own personal view. However, I would like to point out that establishing accounting and auditing standards was a good initiative made by the Ministry of Commerce and strong cooperation is needed between the Ministry and all accounting practitioners to put what have been published so far into practice and work together to

¹⁰ According to one of its senior accountants (Mr Salem), this department currently hires accountants from private accounting firms even to carry out its basic duties (i.e to review financial statements of public companies), let alone ensure the implementation of the accounting and auditing guidelines.

introduce further standards for financial reporting in Saudi Arabia."

Thus, it could be concluded that the lack of an enforcement body and institutional support, together with lack of cooperation from the interested parties, are believed to be the main reasons for the delay in implementing the accounting and auditing guidelines. In addition, the author believes that, because these guidelines include many technical aspects, a special accounting body should be established to monitor their full implementation, and to review and amend them if necessary.

Finally, public accountants in Saudi Arabia seem to have little enthusiasm for improving the accounting profession in the country. Although 51 percent of the public accountants surveyed agreed that the project of developing accounting standards should continue, evidence showed that their contribution so far in this project is very small.

At the end of the questionnaire, respondents were invited to suggest any measures which may be necessary for improving the accounting profession. Although the respondents gave various measures, there was general agreement upon the urgent need for the creation of accounting professional body as well as local training programme, particularly for new accountants entering the profession.

5.6.3 Findings of the Empirical Survey

The main findings of the empirical survey can be summarised in the following points:

1. Public accountants in Saudi Arabia have a variety of experience, which contributes to the diversity in accounting practice.

2. There are various accounting standards found in Saudi Arabia, mainly the USA and the UK standards, and IASs. However, the IASs are widely used in practice.

3. The absence of national uniform accounting standards is believed to be the main reason for the spread of foreign accounting standards in Saudi Arabia.

4. The language and content of auditors' reports differ greatly from one accounting firm to another (see pp.163-164).

5. Shortage of qualified accountants and weakness of internal control systems are considered by public accountants as the most serious problems currently facing Saudi corporations.

6. Auditing, and advice relating to income tax and Zakat are the two most important services provided by the accounting firms in Saudi Arabia. Management advisory services presumably are not in great demand at the present time.

7. Very few local professional accountants participated in the establishment of the recent accounting and auditing guidelines.

8. The problem of enforcement and institutional support, together with lack of cooperation from the

interested parties, are believed to be the main reasons for not fully implementing the accounting and auditing guidelines established so far.

5.7 Summary and Conclusion

The purpose of this chapter has been to examine the main features of the accounting profession in Saudi Arabia. Particular emphasis has been given to the 1974 Law of Certified Accountants, as this was the first law to regulate accounting practice in Saudi Arabia. In addition, the environmental factors affecting the development of accounting practice in Saudi Arabia were discussed. These include type business ownership, foreign influence, rapid economic development, government laws and regulations, and the Saudi Accountants Association (SAA).

The second part of the chapter was devoted to an analysis and discussion of the results of the empirical study which was designed to examine some practical aspects of current accounting practice in Saudi Arabia. For example, it included, among other things, type of accounting standards widely used, reasons for such, type of accounting services and the role of local accountants in recent accounting developments.

In conclusion, the accounting profession in Saudi Arabia is still in its infancy. For all practical purposes, 1974 may be considered as the date of its real origin. The accounting profession has not developed sufficiently to keep pace with the rapid economic

development which has occurred during the last two decades. Its future development hinges very much on an effective professional body setting qualifications and carrying out enhancement activities.

The major deficiencies of the accounting profession are the absence of a professional body, local accounting principles, code of ethics, and institutional support. The Higher Committee of Certified Accountants which now monitors the accounting profession is unable to fulfil its role for the reasons discussed earlier in this chapter. Although there has recently been a move toward the advancement of the accounting profession, these efforts mainly come from foreign accounting experts and local accounting academics, with very little involvement on the part of the local practising accountants (see chapter 9).

Given these facts, it is safe to say that to develop the accounting profession in Saudi Arabia by means of introducing more accounting and auditing standards for external financial reporting on the line of the USA and the UK experiences, would be a very complex process at this stage and unlikely to satisfy the current socio-economic development needs of the country.

CHAPTER 6

ENTERPRISE ACCOUNTING IN SAUDI ARABIA

6.1 Introduction

In recent years a number of business enterprises have been established in Saudi Arabia as a result of the rapid development in almost every economic sector. These enterprises take various forms, ranging from General Partnership (private company) to Corporation (public company). The latter is the largest type of business enterprise found in Saudi Arabia in terms of capital (see table 6.2).

In such large enterprises, accounting is a very significant function; they employ qualified accountants and use a modern book-keeping system. Moreover, in most of them, there is an accounting department whose main function is to record transactions and report on financial statements.

However, the financial reporting of Saudi corporations has recently come under heavy criticism in the local press from both academics and accounting professionals. For example, a number of articles and comments were published in Al-Yamamah (a leading Saudi weekly magazine) criticising the financial reports prepared and published by these enterprises, on the grounds that the information contained in such reports is misleading, inadequate, poorly presented, and, above all, not homogeneous.¹

¹ See Al-Yamamah, particularly issues No. 1028, 1065, 1070, and 1072 for 1989.

Thus the purpose of this chapter is to examine the main features of the existing accounting systems of these corporations, with special reference to those operating in the industrial sector, and to highlight these problems and the main factors which may have caused them. Moreover, considering the extensive economic activities undertaken by them, it would be useful to examine the relationship of their accounting systems to the national accounts, to ascertain whether they provide accounting information relevant to the construction of national accounts. However, before examining their accounting systems, it is necessary to provide a brief background to corporations, showing how they developed and their importance to the national economy.

6.2 Background to Saudi Corporations

6.2.1 Definition

The Companies Law defines a corporation as "A company contracted upon a certain capital divided into equal shares without naming of shareholders."

In addition, the Law sets forth the following characteristics of a corporation:

- 1) It is composed of five or more individuals or entities;
- 2) Its capital is divided into negotiable shares of an equal amount;
- 3) Shareholders are liable only to the extent of the value of their shares;

- 4) Capital cannot be less than SR 2 million - or less than SR 10 million if shares are offered for public subscription;²
- 5) The par value of each share cannot be less than SR 50;
- 6) Paid-up capital at incorporation cannot be less than 50 percent of the authorized capital; and
- 7) The amount payable on subscription must not be less than one-quarter of the total.

6.2.2 Establishment Procedures

Unlike other types of business enterprise, corporations can be incorporated only with a permit granted by Royal Decree promulgated on the approval of the Council of Ministers and a proposal of the Minister of Commerce. The application for such permit must be signed by no less than five shareholders. The application must show the manner of subscription, the number of shares reserved for promoters themselves and the amount subscribed by each one of them. In addition, a copy of the company's memorandum of association and of the articles of association, signed by the shareholders and the promoters, must be attached to the application (Art. 52).

The application is then submitted to the Minister of Commerce, who in turn submits it to the Council of Ministers. If the Council of Ministers approves the application, it will be forwarded to the King, who will issue a Royal Decree authorizing the Company's incorporation.

² These figures were formerly SR 200,000 and SR 1,000,000 respectively.

Since 1982, however, the approval of the Council of Ministers has been transferred to the Minister of Commerce except for:

- Concessionary companies
- Companies administering a public utility
- Companies that receive state subsidies
- Companies in which a state organisation takes part
- Companies doing banking business.

Invitation for public subscription for a company's shares must be made via banks designated by the Minister of Commerce. The invitation takes place by means of a prospectus stating in detail the following particulars (Art. 55):

- 1) Names, domiciles, professions and nationalities of the promoters;
- 2) The company's name, its objectives, and the locations of its head office;
- 3) The amount of paid up capital stock and shares defined as to kind, value and number, the part of such shares subscribed by the promoters, and the restrictions to which transfer of shares is subject;
- 4) Details of shares in kind and their associated rights;
- 5) Privileges granted to promoters or others;
- 6) Method of profit distribution;
- 7) An estimate of the incorporation expenses;
- 8) Commencement and termination dates, locations for and terms of subscription;

- 9) The method of distribution of shares to subscribers to be adopted in the case of over-subscription;
- 10) The commencing date of the Royal Decree authorising the company's incorporation, and the edition of the Official Gazette in which it was promulgated.

The prospectus should be advertised in a daily newspaper circulating in the locality in which the company's head office is situated, not less than five days prior to the commencement date fixed for public subscription (Ibid).

6.2.3 Management

The corporation is managed by a Board of Directors with at least three members, each of whom shall hold a number of shares with value not less than ten thousand Saudi Riyals, to be deposited in his name within thirty days of his appointment date. The maximum term of office for a board member is three years, but he is eligible for re-election unless otherwise provided in the articles of association (Arts. 66-68).

The general meeting of shareholders has supreme power over corporate matters. However, it governs only matters that fall under the commercial code or the articles of association. A General Meeting must be convened at least once a year, within six months after the fiscal year end. Additional Ordinary General Meetings may be convened where necessary (Art. 84)

The Board of Directors must, at least sixty days before the convening of the Annual General Meeting,

prepare for every financial year a balance sheet, a profit and loss account and a report on the company activities, its financial situation and the proposed method of allocating the net profits. These must be signed by the chairman of the Board of Directors and made available for inspection by the shareholders at least fifty five days prior to the day set for the General Annual Meeting (Art. 123).

6.2.4 Sources of Finance

The corporation draws its finance mainly from individual shareholders. The government also contributes in nearly half of the registered corporations (currently 67). The government shares range from less than 25 percent to more than 50 percent (see table 6.1).

Table 6.1
Government Share in Registered Corporations
(as at the end of 1989)

Government %	No. of corporations
- Zero share	34
- Less than 25%	6
- Between 25% to less than 50%	13
- More than 50%	14
Total	67

Source: Compiled from "A Guide to Saudi Corporations" Published by the Council of Saudi Chambers of Commerce and Industry, Riyadh, December, 1989.

In addition, other sources of finance may be raised through the issue of negotiable and indivisible debentures of equal value (Art. 116). In this respect,

the Company Law specifies that the issue of debentures by a corporation should comply with the following terms (Art. 117):

- 1) It must be in accordance with the authorisation for such an issue contained in the articles of association.
- 2) A consenting resolution must be passed by the General Meeting of shareholders.
- 3) The company's capital stock must have been paid up in full.
- 4) The value of the debenture-stock must not exceed the value of the paid-up capital stock.

However, the above terms do not apply to Real Estate Mortgage Corporations, Agricultural or Industrial Mortgage Banks and to the companies exempted by authorisation of the Minister of Commerce (Ibid).

The public may be invited to subscribe for debentures by means of a prospectus bearing the directors' signatures and stating in detail the following particulars (Art. 119):

- 1) the General Meeting resolution on the issue, and its date of publication;
- 2) the number and value of debentures to be issued;
- 3) the date of commencement and termination for subscriptions;
- 4) the debentures' date of maturity, the terms of redemption and the security pledged;
- 5) the value and the security pledged concerning previously issued debentures and the part of them remaining unredeemed on the date of the subsequent issue;

- 6) the company's capital stock and the part paid up thereof;
- 7) the company's head office, date of incorporation and term of duration;
- 8) the value ascribed to contributions in kind;
- 9) a summary of the latest balance sheet.

6.2.5 Alteration of Capital

The Companies Law permits an Extraordinary General Meeting of the corporation to increase or decrease its capital, under certain conditions. Article 134 stipulates that "An Extraordinary General Meeting may pass a resolution to increase the company capital one or more times, provided that the initial capital has been paid up in full". Such an increase may be accomplished by any of the following methods (Art. 135):

- 1) by issuing additional shares, payable in cash;
- 2) by issuing additional shares, representing contribution in kind;
- 3) by issuing additional shares to consolidate specific company debts about to fall due;
- 4) by issuing bonus shares to a total value equal to such reserve surplus as has been resolved by the Extraordinary General meeting to be converted into corporate stock; or by enhancing the par value of all negotiable shares proportionately, commensurate with the said surplus;
- 5) by conversion of promoter's shares or negotiable debentures into corporate stock.

With regard to capital reduction, Article 142 stipulates that "the Extraordinary General Meeting shall be authorized to pass a resolution for the reduction of corporate stock, if the capital is in excess of the company's needs, or in case of sustained losses...". The

reduction of company capital may be effected by any of the following methods (Art. 144):

- 1) by partial repayment of shares or complete or partial release from the duty to pay for shares that are not yet paid up;
- 2) by reduction of a share's par value in proportion to the loss sustained by the company;
- 3) by annulment of a number of shares together amounting to the reduction required;
- 4) by purchase of a number of shares constituting a value equal to the reduction requirements.

In case the reduction of corporate stock shall be established by purchase and subsequent annulment of a number of a the company's shares, the company must appeal to its shareholders to offer their shares for sale by advertising in a newspaper circulating in the municipality in which the company's head office resides (Art.146).

6.2.6 Dissolution

The Companies Law indicates the circumstances which may lead to the termination of a corporation as follows (Arts. 147-48):

- 1) the ownership of all its shares by a single shareholder;
- 2) the number of shareholders falling short of the minimum requirement prescribed in Article 48 (five shareholders);
- 3) losses totalling three quarters of its capital;
- 4) expiration of the corporation's specified duration;
- 5) achievement of the purposes or the impossibility of attaining the purposes of the corporation;

6) agreement among shareholders to terminate the corporation prior to the end of its term unless otherwise specified in the articles of association;

7) merger with another corporation.

Whatever the circumstance which led to the termination of a corporation, the resulting resolution must be advertised in the Official Gazette in accordance with the provisions of article 65 of the Companies Law.

6.3 The Development of Corporations

The first corporation in Saudi Arabia, called the "Arabian Company for Vehicles", was established in 1354H (1934).³ The main purpose of its establishment was transportation of pilgrims to and from the holy places within the Kingdom. However, it was only after the discovery of oil that the number of corporations increased rapidly. In 1956 the first corporation in the financial sector, Riyadh Bank, was established. The first two corporations with foreign equity participation were Arab Petroleum Services, in 1960 and the Arab Petroleum Exploration Company in 1963. By 1965 the number of corporations reached seventeen. The next ten years saw the establishment of a further thirty corporations, and as at the end of December 1989, the number of corporations stood at 67, with a total capital of more than forty five billion SRs (see table 6.2).

³ This corporation later became a private establishment owned by a single individual.

Several factors have led to this increase in the number of corporations, among which are (Riyadh Chamber of Commerce and Industry, 1989, p.80):

- 1) the increase in cash held by individuals;
- 2) The interest of businessmen in participating in the economic activities of the Kingdom;
- 3) the availability of many economic opportunities which offer very good returns;
- 4) the interest of individuals in keeping their wealth as a deposit in banks and their desire to invest them usefully from a religious point of view;
- 5) Government support in terms of incentives and subsidies.

6.4 The Importance of Corporations to the National Economy

The importance of corporations to the national economy stems from the fact that they have a large amount of invested capital which enables them to undertake extensive economic activities. As Shinawi (1970, p.95) stated:

"Corporations are beginning to assume a significant role in the developing economy of Saudi Arabia because of their capacity to raise much more funds and carry out larger industrial and commercial projects needed for development than any other forms of business".

Another feature is that they are the only type of enterprise that is permitted by the Companies Law to engage in insurance, savings and banking activities. Table 6.2 breaks down companies operating in Saudi Arabia by number and paid up capital as at the end of 1989.

Table 6.2
Number of Registered Companies in Saudi Arabia
(as at the end of 1989)

Nature of Enterprise	No.	%	Capital in Million SR	%
1. Corporations	67	1	45,490	57
2. Limited Liability Companies	3755	57	29,842	37
3. General Partnerships	2048	31	3,297	4
4. Limited Partnerships	723	11	1,336	2
5. Partnerships Limited by Shares	1		1	
Total	6594	100	79966	100

Source: Compiled From SAMA's Annual Report (1989)

According to Table 6.2 the total number of business enterprises up to the end of 1989 reached 6,594 with capital around SRs 80 billion. Corporations (67) accounted for 57 percent of total capital, followed by Limited Liability Companies, with 37 percent.

The table also shows that, although corporations represented only 1% of the total number of enterprises registered in the Kingdom as at the end of 1989, their total capital represented 57% of the overall capital.

6.5 Features of the Accounting Systems of Saudi Corporations: Results of the Empirical Survey

6.5.1 Objectives and Approach

The main purpose of this empirical survey was to examine the basic features of the current accounting systems of Saudi corporations and the type of accounting information provided. Matters investigated include general features of the accounting systems, accounting reporting practices, the extent of use of accounting techniques for planning and control, relationship to national accounts, accounting manpower problems and other related issues. The data were obtained by means of questionnaires submitted to twenty-five corporations operating in the industrial sector. The questionnaire was used as the main source of data in this chapter because these enterprises were located in various regions of the Kingdom. Given the distance between these regions and practical considerations such as time, finance, and facilities, it was difficult for the author to interview personally the financial manager of each enterprise.

In addition, reviews were carried out of published financial reports of the enterprises in question and of relevant government laws and regulations. Interviews with the top officials of the Companies Department (including the chairman) at the Ministry of Commerce were also conducted to discuss special issues.

6.5.1.1 Industrial Sector as Fieldwork

As stated above, the total number of corporations stood at 67 at the end of 1989. They operate under five major economic sectors, namely: Industrial, Services, Financial, Electrical, and Agricultural (see figure 6.1).

The industrial sector was selected as the subject of fieldwork for this study for the following reasons:

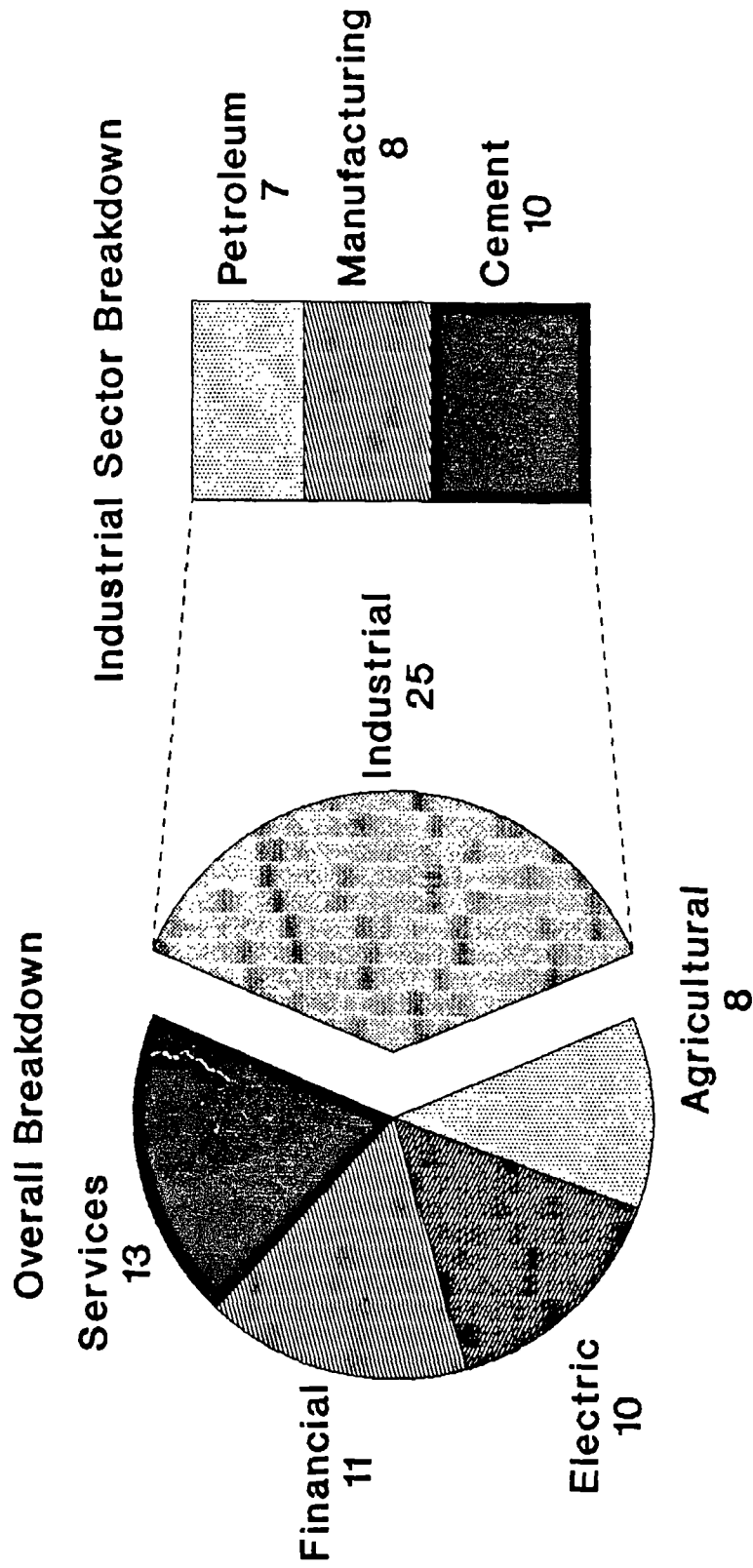
1) The industrial sector has more corporations than the other sectors.

2) The prospective role of the industrial sector in the national economy is considerable. The Government has always adopted a forward-looking policy and views industrialization as the base upon which the economic and social well-being of future generations can be maintained, even when oil resources have been drained.⁴

3) Concentrating on a group of enterprises in one sector facilitates the task of analysis and evaluation of accounting systems, since all of them have similar operations.

⁴ The Government provides the Industrial Sector with interest-free loans from the Saudi Industrial Development Fund (SDIF), land free of charge, exemption from tax on imported materials, etc.

Figure 6.1
 Breakdown of Saudi Corporations by
 Economic Sectors as at the End of 1989



Source: Compiled from A Guide for Saudi Corporations, Saudi Chambers' Council, Riyadh, 1989.

Table 6.3 shows the names, paid up capital and total assets of the 25 industrial corporations participated in this study.

Table 6.3
Industrial Corporations Participated in the Study
(Value in Million SR)

Sector/Company Name	Paid up Capital		Total Assets	
	Value	%*	Value	%*
[A] Cement				
1. Arabian Cement Ltd Co.	600	12	1016	12
2. Saudi Cement Co.	420	8	693	8
3. Alyamamah Cement Co.	885	17	1188	14
4. Gaseem Cement Co.	300	6	696	8
5. Yanbu Cement Co.	525	10	825	10
6. Southern Cement Co.	700	13	975	12
7. Saudi Bahrain Co.	895	18	1180	14
8. Saudi Kuwait Cement Co.	645	12	1367	16
9. National Gypsum Co.	72	1	127	2
10. Saudi Ceramics Co.	150	3	271	3
Total	5192	100	8338	100
[B] Petroleum				
1. Arabian Refineries Co.	24.0	4	61	1
2. Petroleum Equip. Trading Co.	6.0	1	266	2
3. National Gas & Manuf. Co.	500.0	79	991	7
4. BETROMIN for oil Co.	15.5	2	337	3
5. Marine Constructions Co.	0.5	0	33	0
6. Arabian Digging Co.	20.0	3	62	1
7. Jeddah Oil Refineries Co.	70.0	11	11189	86
Total	636.0	100	12939	100
[C] Manufacturing				
1. Saudi Fertilisers Co.	200	2	1610	5
2. SABIC.	5000	87	26955	89
3. Saudi Pharmaceutical Co.	150	2	244	1
4. National Manufacturing Co.	300	4	355	1
5. Edible & Veg. Oil Co.	120	1	296	1
6. Saudi Cables Co.	270	3	900	3
7. Advanced Industry Co.	27	0	29	0
8. Glass Industries Co.	25	0	33	0
Total	6092	100	30422	100

* Percentages in this table are rounded.

Source: Compiled from Saudi Corporation Guide, Saudi Chambers' Council, Riyadh, December, 1989.

6.5.1.2 Questionnaire Design and Procedures

The questionnaire was divided into four parts (see table 6.4). Part one surveyed the background of the respondents, while part two examined the main features of the accounting system of the enterprise, including general features (e.g the design of the system, data processing method, chart of accounts, financial reports currently prepared, their frequency and their users); rules, methods, and principles in practice; and the extent of use of accounting techniques for planning and control purposes. Part three concentrated on information related to the construction of national accounts and the social responsibility of corporations. Finally, part four dealt with accounting manpower problems and other related issues.

Table 6.4
The Questionnaire Structure

Part No.	Title	No. of Qs.	Sequence
1	General Data	10	1-10
2	Features of Accounting System: A> General Features B> Reporting Practices C> Planning and Control	12 12 9	11-22 23-34 35-43
3	Relationship to National Accounts	8	44-51
4	Accounting Manpower Problems & Related Issues	9	52-60

The questionnaire was mailed or handed to the financial managers of each of the 25 industrial corporations. Each financial manager was sent a large

envelope containing a covering letter explaining the main purpose of the study and setting forth guidelines for completion of the questionnaire, the questionnaire itself, and a self-addressed stamped envelope for returning the questionnaire. In addition, a letter from the Dean of the Faculty of Economics and Administration was enclosed to introduce the researcher to the participants and encourage them to cooperate.⁵

Special procedures were adopted to ensure that each enterprise in the sample received the survey package. For this purpose the enterprises were divided into two groups: the first group constituted those enterprises (7 in number) which operated in Jeddah. Each enterprise in this group was given the survey package either by the author or his friends. A date for collecting the questionnaire from this group was also agreed at the time of delivery.

The second group constituted those enterprises (18 in number) located in other parts of the country. After discussion between the researcher and his internal supervisor (in Saudi Arabia), it was decided that the best way to send the survey package to these enterprises was through the official (Government) mail. Thus, contact was made with the communication centre of King Abdul Aziz University (the researcher's employer) and special forms were completed which included the name and address of each enterprise and destination. Then, all the envelopes,

⁵ Copy of the questionnaire is reproduced in Appendix B.

together with these forms, were submitted to the communication centre and a signature was obtained.

Although the above procedures seem rather complicated, the outcome was remarkable as all the questionnaires were returned within a reasonable time. Moreover, responses were generally thoughtful and complete: very few respondents left any questions unanswered, and many used much more than the answer spaces available in the questionnaires. Where useful to illustrate the results below, selected respondents' views are quoted.

6.5.2 Respondents' Background

The first part of the questionnaire (Qs.1-10) dealt mainly with four major areas: citizenship, educational background, place of education, and experience in accounting and finance. It also provided basic data concerning the enterprise under investigation.

As expected, the survey revealed that most of the financial managers of the Saudi industrial corporations were Saudi nationals; only six were not (three Egyptians, two Jordanians and one Sudanese).

As for the educational qualifications of the respondents, the survey showed that 4 respondents held a master's degree, one held a higher diploma in cost accounting and 20 held a bachelors degree. Only one respondent had ACA from England. With regard to place of education, 12 of the respondents received their degrees from Saudi universities, 10 from Arab countries (mainly

Egypt) and the remaining 3 from foreign countries (USA and UK). The majority of the respondents (18) had more than five years experience in accounting and finance. Moreover, nearly all the respondents acknowledged that accounting plays a very important role in an enterprise.

6.5.3 General Features

6.5.3.1 Design of the accounting system

Question 11 sought to determine the body that designed the accounting system of the enterprises concerned. Responses to this question, shown in table 6.5, indicate that in 8 corporations, the accounting system was designed by the accountants of the enterprise itself. In 5 corporations, it was designed by a Saudi accounting firm and in 9 others by a foreign accounting firm. The remaining 3 respondents stated that their accounting systems were designed by a combined effort between the enterprise's accountants and an outside consultant body.

Table 6.5
Design of the Accounting Systems of Corporations

Designing body	No.
a. Accountants of the Enterprise	8
b. Saudi Accounting Firm	5
c. Foreign Accounting Firm	9
d. Other	3
Total	25

It should be noted that most of the enterprises whose accounting system was designed by a foreign accounting firm were established prior to 1980. This perhaps reflects the fact that at that time, there were comparatively few Saudi accounting firms which could offer accounting services such as system design.

6.5.3.2 Data Processing Methods

Accounting systems in common use range from manual systems, which use a special journal to streamline the posting process, to sophisticated computer systems. However, the data processing system in any given enterprise depends, among other things, upon the volume of information involved. In question 12, respondents were asked to indicate the data processing methods they used. Responses to this question are shown in the following table.

Table 6.6
Data Processing Methods Used By Corporations

Data Processing Methods	No.
a. Manual	3
b. Mechanical	4
c. Computer	6
d. Combination of a, b and c	12
Total	25

The overall results show that 12 of the corporations used a combination of data processing methods, including manual, mechanical and computer. Only 6 stated that they

currently used computer alone in the payroll and inventory control. However, most of the respondents pointed out that they were in the process of computerising their accounting system, or hoped to do so in the near future. Perhaps this delay may be attributed to the shortage of qualified operators.

6.5.3.3 Charts of Accounts

Accounting transactions must be classified and coded before being posted to ledgers. A chart of accounts is a coded listing of the accounts contained in the general ledger of a firm.

In question 13, the respondents were asked if their enterprises currently had a chart of accounts. Only 10 of them indicated that they did, while the remainder did not.

It is surprising that so many enterprises do not yet have a chart of accounts, for such a chart not only enables transaction data to be classified and coded, but also provides the detailed data elements from which information can be assembled and presented in financial reports. The usefulness of the chart of accounts has been emphasized recently by Cushing and Romeny (1990, P.78) who stated:

"The chart of accounts is an extremely useful tool for processing accounting data in organisations of all types and size. It facilitates the recording and posting of transactions, and it simplifies the preparation of financial statements and a variety of other summaries."

6.5.3.4 Type of Financial Reports

The Companies Law requires the Board of Directors to prepare for each financial year the following reports (Art. 123):

1. A balance sheet;
2. A profit and loss account;
3. A report outlining the corporation's affairs and its financial position during the preceding financial year, as well as the manner in which it is proposed to distribute the net income.

The Law also lays down deadlines for the preparation and publication of financial reports. It specifies that financial reports and the directors' report should be prepared at least sixty days before the Annual General Meeting, made available to the auditor at least fifty-five days before the meeting and published in a local newspaper at least twenty five days before the meeting.

Furthermore, in a recent circular, the Ministry of Commerce required each corporation to prepare and publish its financial reports in a local newspaper every three months, though this is not yet always strictly observed. Even those enterprises which do publish their financial reports quarterly usually give no more than a summary of the balance sheet and profit and loss accounts, without any further information, except one footnote which indicates that "the above figures are unaudited".

In question 14, the respondents were asked to state the type of financial reports currently prepared by their

enterprises. The answers are shown in the following table.

Table 6.7
Financial Reports Currently Prepared

Reports	No.
a. Balance Sheet	25
b. Profit and Loss	25
c. Directors Report	25
d. Sources and Application of Funds	8
e. Changes in Financial Position	5

It is thus clear that all 25 enterprises comply with statutory requirements concerning the preparation of a balance sheet, profit and loss account, and directors' report. However, other reports such as statement of source and application of funds and changes in financial position are not commonly prepared, despite their importance. It was also found that the enterprises in question gave comparative figures for only two periods, the present and the preceding year. However, this is not very sound from a time-series analysis point of view, because such a short period may not reveal trends or may have been distorted by individual events.

It should be pointed out that the Companies Law does not specify the format of the financial statements, which thus vary considerably. Some corporations use the vertical format which starts with assets classified into current assets (e.g. cash on hand and in banks, accounts receivable, accrued amounts, inventory) and fixed assets

(e.g. property, machineries, equipments) followed by liabilities (classified into current and non-current liabilities) and shareholders' equity (table 6.8); while others use the T-account format which shows current assets first, followed by fixed assets minus accumulated depreciation in one side and current liabilities followed by shareholders' equity on the other side (table 6.9). Diversity in published financial statements has become a common phenomenon in recent years, and a number of people have expressed their concern about this (see Al-Yamamah, issue No. 1028, 1989, p.47).

Table 6.8
Saudi Cables Co. (Saudi Public Corporation)
Balance Sheet As At December 31, 1989

<u>ASSETS</u>	Note	1989 (000) SR	1988 (000) SR
Current Assets			
Cash on hand and in banks		69,930	52,453
Accounts receivable and prepayments	3	249,545	230,022
Accrued amounts from associated Comps.		27,720	6,698
Inventory	4	148,218	162,676
		<hr/>	<hr/>
		495,413	451,849
Accrued receivable balances		39,396	32,672
Investments in subsidiary and associated companies	5	59,676	37,085
Other Investments	6	29,926	21,110
Postponed Expenses	7	37,367	31,232
Fixed Assets			
Property, machineries & equipments	8	335,485	328,099
		<hr/>	<hr/>
Total Assets		997,263 =====	902,047 =====
<u>Liabilities and Shareholders' Equity</u>			
Current Liabilities			
Accounts payable & Accrued Amounts	9	125,522	88,932
Amounts Received in advance		6,199	12,416
Accrued amounts to associated Comps.		4,086	7,924
Short-term Loans	10	195,277	112,500
Accrued instalments		65,139	66,338
		<hr/>	<hr/>
		396,223	288,110
Non-Current Liabilities			
Long-term Loans	10	226,519	266,402
Accrual end-of-severance Benefits		17,246	15,191
		<hr/>	<hr/>
Total liabilities		640,168	569,703
Net Shareholders' Equity			
Share capital	11	270,000	270,000
Statutory reserve	12	57,157	55,671
Retained earnings	13	29,938	6,673
		<hr/>	<hr/>
Total Shareholders' Equity		357,095	332,344
Total Liabilities & shareholders' Equity		997,263 =====	902,047 =====

Source: Saudi Cables Corporation, Annual Report, 1989
(author's translation).

Table 6.9
National Industries Co.
(Saudi Public Corporation)
Balance Sheet As At December 31, 1989

	Note	1989	1988	Current Liabilities	1989	1988
Current Assets						
Cash in banks	1	25,222,047	14,424,219	Accounts payable	10,085,541	5,042,003
Cash in Riyadh Bank		4,419,050	---	Other payable	4,419,050	15,000,000
Accrued revenues	2	3,634,061	8,718,902	Accrued expenses	1,127,262	687,717
Various receivable		2,497,425	3,004,656	Provision for legal Zakat	357,094	3,718,491
Employees Receivable		224,248	40,286	Provision for employees terminal benefits	2,890,252	1,977,311
Bank guaranties		---	7,500			
Expenses paid in advance		862,162	947,675			
Total Current Assets		36,858,993	27,143,238	Total current liabilities	18,879,199	26,425,522
Projects under study	3	11,639,386	13,603,781	Shareholders' Equity		
Projects under establishments		---	8,263,177	Capital	300,000,000	300,000,000
Investments in other companies	5	310,711,128	256,012,054	Legal reserve	7,157,620	5,287,047
Other investments		1,185,884	48,309,492	Conventional reserve	5,510,057	6,906,055
Short-term loans		3,430,000	750,000	Accumulated profits	18,719,143	17,213,016
Fixed Assets		3,070,423	2,793,967	Profits appropriated for shareholders	15,000,000	---
Less Accumulated depreciation	6	(1,629,795)	(1,044,069)			
Net values of fixed assets		1,440,628	1,749,898	Total Shareholders' Equity	346,386,820	329,406,118
Total Assets		365,266,019	355,831,640	Total liabilities and Shareholders' Equity	365,266,019	355,831,640

* Attached Notes from No. (1) to No. (18) form an integral part of the financial statements.

Source: National Industries Corporation, Annual Report, 1989 (author's translation).

6.5.3.5 Frequency of Financial Reports

To be useful for decision-making, financial reports should be prepared and published in reasonable time, otherwise the information which they contain would be out-of-date. The survey shows that all the respondents comply with statutory requirements by preparing and publishing their financial reports annually. Also, all of them comply with the recent circular of the Ministry of Commerce and publish a summary of their financial reports quarterly. Only four of the enterprises surveyed prepare additional reports on a monthly basis for internal use, and supplementary accounting information other than financial reports is not prepared. For example, no information is provided on value added, money exchange with government, employment, analysis of financial ratios (e.g. earnings per share or return on capital), efficiency of production department and utilization of production capacity.

6.5.3.6 Users of Financial Reports

Due to the lack of empirical study concerning the users of financial reports in Saudi Arabia, a list of potential users was provided and the respondents were asked to rank these users from 1 to 6, using 1 to indicate the main user group and 6 to denote the least important users. Responses received are tabulated and discussed below.

Table 6.10
Users of Financial Reports

Users	Rank	No.
a. Owners (Shareholders)	[1]	21
b. Department of Zakat and Income Tax	[2]	20
c. Saudi Industrial Development Fund	[3]	18
d. Commercial Banks	[4]	16
e. Ministry of Commerce	[5]	12
f. Employees	[6]	8

The overall results show that the shareholders of an enterprise are ranked as the main users of financial reports. It should be pointed out that, although it is accepted that financial reports are prepared for use mainly by shareholders, the figures contained in the reports may nowadays reach such a degree of complexity that the shareholders in many cases do not understand them. It is quite possible that many figures are published in the name of shareholder information, when they are only understood by financial analysts and other accountants. This is true even in developed countries, let alone the situation in Saudi Arabia where private shareholders lack education and experience. Support for this view is derived from the survey conducted in the UK by Lee and Tweedie (1977). They found that annual reports appear to be used thoroughly by a minority of private shareholders and that their comprehension is not at a particularly high level.

According to response ranking, the Zakat and Income Tax Department (ZITD), Saudi Industrial Development Fund (SIDF), Commercial Banks and Ministry of Commerce came in the second, third, fourth and fifth places respectively. This ranking was expected as the ZITD is the only tax jurisdiction in the country; the SIDF provides medium and long-term loans to the Saudi industrial enterprises; the commercial banks provide short-term credit to various enterprises; and the Ministry of Commerce is the government body which regulates and monitors all enterprises in the country. However, employees are ranked as making least use of financial reports.

6.5.4 Accounting and Reporting Practices

The objective of this section is to review accounting policies as reported by the respondents regarding fixed assets measurement and depreciation, valuation of stock, revenue recognition, treatment of Research and Development expenditures, foreign currency transactions and accounting for inflation. To illustrate how these items are treated in practice, extracts from the financial reports of the companies under examination are given below. Although items discussed here are not comprehensive, they are those most commonly encountered in the preparation of financial reports.

6.5.4.1 Fixed Assets and Depreciation

The survey shows that historical cost is used by most corporations as the basis for recording fixed assets such as buildings, machineries, equipments, vehicles and tracks on financial reports. This was indicated by all respondents. However, it has been argued that the use of historical cost is unsatisfactory for decision-making, particularly when prices are changing (Allardyce, 1983).

"Financial statements are prepared according to the historical cost principle" [Saudi Cables Company, Annual Report, 1989, Significance Accounting Policies, para B].

"The Balance sheet is prepared according to historical cost principle, while revenues and expenses are treated on the a accrual basis" [National Gypsum Company, Annual Report, 1989, Significance Accounting Policies, para C].

As regards depreciation, the straight-line method is widely applied, though a few respondents use other depreciation methods, such as declining balance and percentage of use. Perhaps the reason for the popularity of the straight-line method is that it is simple and easy to apply. It should be pointed out, however, that this method does not reflect that the greatest loss in the market values occurs in the first year of use, nor the diminishing losses in the value which occur in later years, as the asset approaches the end of its useful life.

The annual depreciation charges are calculated using the following formula:

$$D = \frac{C - S}{N}$$

Where D is the annual depreciation
 C is the acquisition cost
 S is the scrap value
 N is the life in years.

The acquisition cost of a fixed asset is comprised of both the purchase price and other directly attributable costs (e.g. costs of handling, delivery, installation of the fixed asset).

In general, the accounting policy adopted in calculating depreciation is disclosed. It is also common to give details of the rates of depreciation used for writing off various categories of fixed assets. These rates are normally based on the estimated useful life of assets, which varied among the enterprises in question. SABIC, for example, gives the following useful lives for its fixed assets:

- Buildings	33 years
- Equipment	20 years
- Furniture and fixtures	4-10 years
- Vehicles and transportation equipments	4-6 years

[SABIC, Annual Report, 1989, Summary of the Significance Accounting Policies, para C].

6.5.4.2 Valuation of Stock

There are several methods for valuing stock, each producing markedly different results. The survey revealed that the lower of cost or market price is used by 16 corporations, while 9 use the cost basis. No other bases were reported to be in use. Classification of stock into raw materials, work in progress, and finished goods is not common among the enterprises including in the survey.

As for computing inventory cost, it was found that the first in first out (FIFO) method is used by the majority of the respondents (18), followed by the weighted average cost method. The FIFO method is based on the artificial assumption that the first goods bought are the first sold. This means that in effect, the stock held at the end of the period is assumed to be that purchased most recently. It is the opposite to the last in first out (LIFO) method, to which none of the respondents referred at all.

"The end period stock is valued at the lower of cost or market price basis" [Arabian Cement Co., Annual Report, 1989, Significance Accounting Policies, para 2.5].

"The company follows the first in first out policy for pricing raw materials, while goods in process and finished goods are valued at actual costs" [Saudi Pharmaceutical Co., Annual Report, 1989, Significance Accounting Policies, para 9].

"- Finished goods are valued at the lower of cost or market price;

- Goods in progress are valued according to the direct cost of material and labour;

- Raw materials, chemical tools and backing tools are valued on the weighted average cost basis" [Edible & Vegetable Oil Co., Annual Reports, 1989, Significance Accounting Policies, para C].

It should be pointed out that these methods are used voluntarily, since there are no local requirements as such.

6.5.4.3 Revenue Recognition

It is usually acknowledged that revenue and income are earned throughout stages of the operating cycle (i.e. during order reception, production, sale, and collection). The problem is how to allocate revenue and income to the different stages of the operating cycle. In order to overcome this problem, accountants employ the realisation concept to select critical events in the cycle for the timing of revenue and the recognition of income. The realisation concept states that revenue is recognised in financial statements in which (1) the earning process is complete or virtually complete and (2) an exchange has taken place (APB Statement No.4, 1970).

There are no local requirements for the disclosure of the basis for recognising revenues. Although all the 25 corporations surveyed use the accrual basis of accounting, they differ in the point at which they recognise revenues. For example, 17 corporations use the sales point, 6 use delivery point and 2 use the production point.

"Revenues are recognised when delivery of products is made to costumers" [Saudi Ceramic Company, Annual Report, 1989, Significance Accounting Policies, para 2].

With regard to revenues from investments in other companies, the survey shows that such revenues are normally recognised when they are declared by the subsidiary companies according to their latest audited financial reports.

6.5.4.4 Research and Development

Again, there are no local requirements for the treatment and disclosure of research and development expenditure. However, the survey revealed that only five corporations have a research and development cost centre. In only two of the five are the research and development costs directly capitalized. In the remaining three, the costs are expensed in the year in which they are incurred.

It should be pointed out that accountants have different views concerning the treatment of research and development costs. In the USA, for example, all research and development costs are expensed as they are incurred (see FASB Statement No.2), while in the UK, the treatment of such costs is more flexible: general research must be expensed immediately, but research involved in refining and developing a specific product may be treated as an asset and expensed over its economic life (see SSAP 13).

6.5.4.5 Foreign Currency Transactions

Almost all business enterprises in Saudi Arabia are involved in foreign currency dealings, because most goods and services are imported from other countries. However, it is not common to find disclosure of the accounting policy in respect of foreign currency transactions, for there is no local requirement for their treatment and disclosure. However, the common accounting policy, based on review of the published financial reports of the enterprises in question, appears to be as follows:

"Transactions involving foreign currencies are translated to Saudi Riyals at rates prevailing at the dates of such transactions. All assets and liabilities recorded in foreign currencies are translated at the rates of exchange prevailing at the balance sheet dates. Any gains or losses resulting from translation are treated in the income statement." [Edible & Vegetable Oil Co., Annual Reports, 1989, Significance Accounting Policies, para H].

The above statement seems to comply with the requirements of IASs 21, "Accounting for the Effects of Changes in Foreign Exchange Rates".

6.5.4.6 Inflation Accounting

There is no local requirement for the production of inflation accounting, though the recent accounting statement, which is at present in the process of becoming mandatory, touches upon the subject of inflation accounting when it states (para 374) that:

"moderate changes in the purchasing power of the Saudi Riyal, if continuing for many years, and considerable changes that continue for short periods, require restatement of financial statements in order to reflect changes in the general level of prices."

In our survey, only three respondents indicated that changes in price were considered when preparing financial reports. Two out of the three applied the replacement cost approach and the other used current cost accounting. No other methods of accounting for inflation, such as general purchasing power, were reported to be used. In fact, it should be noted that there is no universally accepted standard for inflation accounting.

6.5.5 Reason for Diversity in Reporting Practices

The major conclusion of the above section is that annual reports prepared by these corporations are diverse, due to the absence of local requirements, since neither the Companies Law nor the Income Tax and Zakat Regulations specify any particular accounting guidelines to be followed, except that article (124) of the Companies Law indicates that:

"A terminology identical to that of preceding years shall be used in the headings of the balance sheet and the profit and loss account, and consistent measures shall be applied to value the assets and liabilities, unless the General Meeting shall pass a resolution to amend said terminology or measures as proposed by the auditor."

However, the Companies Law does not prescribe this terminology, or the layout of financial reports and methods of measurement to be used by accountants when preparing financial reports. Accordingly, the accounting principles adopted by enterprises depend largely on the educational background and professional experience of their accountants.

To clarify this point, respondents were asked about the sources of accounting methods, policies, and principles; and whether they have changed their accounting system during the last five years. The responses show that a combination of written accounting system, personal experience and various laws and regulations are the main sources of accounting methods, policies, and principles in 21 corporations. Moreover, 11

of the respondents stated that they had changed their accounting system during the last five years. Thus, it could be argued that the use of inconsistent accounting methods, policies and principles by corporations, and constant changes in their accounting system, all affect their published financial reports.

6.5.6 Utilisation of Accounting Techniques for Planning and Control

Managers, in their decision-making and control activities, use various cost and managerial accounting techniques, such as budgeting, standard costs, variance analysis, break-even analysis, etc.

In questions 35 and 36, the respondents were asked to indicate whether they used a budgeting system for planning and control purposes and, if so, what type of budget was currently prepared. Responses to these two questions are shown in the following table.

Table 6.11
Use of Budget System and Types
of Budget Currently Prepared

- Use Budgeting System	Yes 23	No 2	= 25
- Types of Budget Currently Prepared			No.
a. Production Budget			21
b. Sales Budget			20
c. Purchase Budget			18
d. Capital Expenditure Budget			16
e. Cash Budget			16
f. Administration Expenses Budget			7

Although the overwhelming majority use a budgeting system for purposes of planning and control, they differ in the types of budget currently prepared. Nearly all corporations prepare and use production, sales and purchases budgets. Capital expenditure and cash budgets are also popular, while the administration budget seems to receive less attention.

With regard to the methods used for long term capital expenditure decisions, 17 corporations stated that they used the payback technique based on the following formula:

$$\text{Payback period (years)} = \frac{\text{Net Investment Outlays}}{\text{Average Net Cash Inflows}}$$

It must be mentioned, however, that although the payback technique has the advantage of simplicity, it ignores cash flows beyond the payback period and the time value of money. Of the remaining eight corporations, five stated that they use discount cash flow technique, two employ accounting rate of return, while one company stated that it depends on outsider consultant body in issue concerning capital expenditure.

A standard costing system is another useful accounting control technique, whereby costs are predetermined and subsequently compared with actual costs. Differences between standard and actual costs are known as variances.

In question 39 and 40, respondents were asked to indicate whether they use a standard costing system and,

if so, whether they analyse variances. Responses to these two questions are shown in the following table.

Table 6.12
Use of Standard Costs and Variance Analysis

- Use of Standard Costs	Yes 9	No 16	= 25
- Variance Analysis			No.
a. Materials Variance			4
b. Labour Variance			2
c. Overhead Variance			3
d. Other			1

Table 6.12 shows that only nine of the twenty-five corporations participated in this study were used standard costs technique for control purposes. It is also clear that analysis of variances is not popular among these corporations. It should be noted that analysis of variances resulting from the utilisation of such technique is particularly important to ascertain whether they are justified or unjustified. If they are justified either because estimates of quantities of input resources or input prices are wrong then the standard costs must be modified. If, however, they are unjustified, then the reasons for these variances must be inquired and right action taken. Moreover, 11 corporations use other forms of cost analysis, such as break-even analysis, and 13 break down total costs into fixed and variable costs.

It can be concluded that the use of accounting techniques for the purposes of planning and control is limited among the enterprises surveyed. This is

attributed to the weakness of the internal control system and the cost accounting system, as well as the shortage of qualified accountants. An interview with Mr. Al-Kharashi, a Certified Public Accountant, supported this conclusion. In answering a question put to him by the economic editor of Al-Yamamah (see issue No. 1072, September, 1989, p.48) concerning the major shortcomings of the accounting systems of corporations, he cited the following:

- 1) Internal control systems are weak.
- 2) The preparation of financial reports is confined to the final accounts and balance sheet, without any other accounting data, with the object either of keeping accounting expenses down, or of hiding information in order to avoid paying Zakat or income tax.
- 3) There is a lack of awareness of the benefits of implementing managerial accounting for decision-making.
- 4) Cost accounting systems in industrial enterprises are weak.
- 5) The educational level of those responsible for financial affairs in many corporations is poor.

6.5.7 Accounting Systems of Corporations and their Relation to National Accounts

The third part of the questionnaire (questions 44-49) was designed to examine the current accounting systems of corporations in respect of the needs of national accounts. The survey revealed that their current accounting systems are little concerned with the information needs of national accounts.

In question 44, respondents were asked whether the current accounting systems of their enterprises have any

link with national accounts. The overwhelming majority of the respondents (22) replied negatively, while the remaining 3 gave positive answers. As for the question of whether the accountants of the enterprise were actually aware of the needs of national accounts, only 5 respondents suggested that accountants are aware of such needs. One respondent commented on this part of the questionnaire as follows:

"Sometimes we receive special forms from the Central Department of Statistics. We fill these forms in and send them back ... we think that information collected by such forms might be used for national accounts purposes, because the forms are headed by the National Accounts Section."

The responses to the question, "What do you think is the main reason for lack of awareness of the needs of national accounts?" are shown in Table 6.13. Here it is clear that the main reason given is the absence of statutory requirements to guide accountants in preparing and publishing accounting information relevant to the construction of national accounts. This is followed by other reasons such as the nature of the present accounting systems of corporations and shortages of accounting personnel.

Table 6.13
Reasons for Lack of Awareness of the Needs
of National Accounts

Reasons	No.
a. Because there is no statutory requirement for the data needed by NAs	12
b. Because the existing accounting system is not designed to provide data for NAs	8
c. Because of the Shortage of Accounting Personnel	5

It was stated earlier that these corporations are the largest business enterprises in Saudi Arabia in terms of capital, and of economic activity. Accordingly, their accounting information is of particular importance for the purpose of national accounts. A list of suggested items (see table 6.14) was provided for the participants, who were asked to confirm whether they disclose such items, either in the main body of the financial reports of their enterprises, or in supplementary reports.

Table 6.14
Items Relevant to the Construction of National Accounts

Items
1> analysis of fixed assets
2> details relating to historical cost - year of purchase - new or second hand acquisition - depreciation rate - expected life
3> classification of stock into: - raw materials - work in progress - finished goods
4> classification of cash between local and foreign currency
5> classification of long-term investments between foreign and local-based
6> the amount of imports
7> the amount of exports
8> value added and its components
9> transfer payments
10> sales of goods to non-residents
11> salaries and wages paid to nonresidents
12> state subsidies
13> increase in physical inventory
14> classification of cash between cash in hand and cash at bank
15> classification of purchases between purchases for sales and purchases for use

The overall result of the survey revealed that on average, less than 4 respondents disclose these items, while the majority of the respondents either responded negatively or simply avoided this question.

It therefore seems reasonable to conclude that the role of the accounting system of corporations in providing accounting information relevant to the construction of national accounts is at best very weak.

As for the social responsibility of corporations, it is extremely difficult to find disclosure of relevant information. The survey revealed that only 6 respondents disclose information such as that listed in the following table.

Table 6.15
Items Related to the Social Responsibility
of an Enterprise

Item	Yes	No
1. Employees' welfare	2	23
2. Donations for social causes	1	24
3. Encouragement of use of Saudi employees	3	22
4. Health and safety protection	00	25
5. Pollution control	00	25

One respondent pointed out that "information concerning the social responsibility of the company is not required to be published in financial reports and our accountants have no experience of such issues". Furthermore, it seems to the researcher that little attention is paid to social responsibility of enterprises, even by officials. For example, when this issue was discussed with the general director of the Companies Department, he simply stated, "If an enterprise does not make profits, there is no point in its

existence". Another official of the Companies Department stated, "Our duty is to ensure that all corporations comply with the Companies law and other related regulations".

6.5.8 Accounting Manpower Problems

Accounting manpower is considered as a part of the overall work-force of any enterprise. Table 6.16 shows the classification of these corporations according to the size of their work-force as at the end of 1989. The table shows that 16 of them have more than 400 employees, 6 between 200 to 400 employees, while only 3 have less than 200 employees.

Table 6.16
Breakdown of Corporations By Number of Employees

Category	No.
a. Less than 200	3
b. Between 200 to 400	6
c. More than 400	16
Total	25

The respondents were asked to state the number of accountants currently employed by their enterprises according to whether they were of Saudi or non-Saudi nationality (part IV, Q.53). The results revealed that the accounting manpower totalled 510 accountants as at the end of 1989. Of these, 204 (or 40 percent) were Saudi nationals. Moreover, 17 of the respondents confirmed that they still face problems in recruiting new accountants.

One of the main obstacles facing new Saudi graduates in joining corporations as accountants is the requirements specified for such a post. For example, most corporations, when advertising an accounting post, normally require that the applicant must have, in addition to academic qualifications, the following:

- 1) an accounting professional qualification from any professional body, particularly those of the USA or the UK;
- 2) at least five years previous experience in accounting and auditing;
- 3) fluency in the English language, both written and spoken.

These conditions can rarely be met by a new Saudi graduate, at least at present. Hence, a number of Saudi writers have argued that these conditions should be reconsidered, particularly that related to the number of years of experience required for an accountant's post. After all, a new Saudi accountant cannot gain such experience if he is not given the opportunity to practise in the first place.

In order to assess the accounting manpower needs of corporations, five accounting fields were identified and the respondents were asked to rank them from 1, for the field which most needs qualified personnel, to 5 for the field which has the least need. The answers are shown in following table.

Table 6.17
Rank of the Accounting Field Needed by Corporations

Accounting Field	Rank	No.
a. Financial Accounting	[1]	18
b. Auditing	[2]	15
c. Cost and Managerial Accounting	[3]	13
d. Specialized and Applied Accounting	[4]	9
e. Taxation and Zakat accounting	[5]	3

It is clear that financial accounting and auditing are the two fields where staff are most considered to be needed. This suggests that more emphasis is placed upon external financial reporting and external auditing than upon the internal needs of the enterprise, which involve the utilization of the cost and managerial accounting techniques referred to above. In order to determine how the companies are tackling the problem of shortage of accountants, respondents were asked whether they have a training programme for their accounting personnel. Only 7 enterprises out of the 25 included in the survey stated that they do provide such training programmes. Two of the seven have their own training centre, while the remaining five stated that their accounting personnel attend a local training programme provided on an occasional basis by the Chamber of Commerce and Industry.

6.5.9 General Implications

In the absence of an official pronouncement of accounting principles and mandatory standard formats of accounting reports, the last two questions of the survey sought opinions on the possible adoption of a uniform accounting system for Saudi enterprises. The majority of the respondents (17) recommended the adoption of a set of rules or principles for classifying and recording accounting data to be applied by all business enterprises in Saudi Arabia. 5 respondents did not favour this, while 3 of them felt that such a system could be adopted for a group of enterprises of identical operations. Of the 17 respondents who recommended adoption, 9 stated that such a system should be established by a team including accounting professionals, accounting academics and government officials. 6 respondents recommended that the Ministry of Commerce should undertake the task, while the remaining 2 advocated that action should be taken by a private accounting body. The first group presumably favoured the action already taken, which involved a number of accounting experts with various backgrounds (see chapter 9).

It must be emphasised that a uniform accounting system, if adopted, will solve a number of problems currently facing Saudi enterprises. For example, it would facilitate the work of the external auditor, because most of the work of accountants would be standardised and there would be very marginal scope for differences in accounting treatments. It would also alleviate the

problem of shortage of accounting manpower and facilitate the training process and transfer of "know-how" and skills (Enthoven, 1973, p.237).

6.6 Summary and Conclusion

The purpose of this chapter has been to examine the current accounting systems of Saudi corporations. This type of enterprise was selected because they are the largest business entities in terms of capital, and of economic activity.

An analytical study based upon a survey questionnaire submitted to 25 Saudi public corporations operating in the industrial sector, as well as a review of their published financial reports, revealed the following main points:

1. There are considerable differences in their accounting systems and reporting procedures, which affect accounting information, in respect of both quantity and quality.

2. The main reason for these differences is the absence of local requirements, since neither the Companies Law nor the Income Tax and Zakat Regulations specify any particular accounting guidelines to be followed.

3. Although all enterprises included in the survey comply with statutory requirements concerning the preparation of a balance sheet, profit and loss account, and directors' reports, other reports such as statement of source and application of funds and changes in

financial position are not commonly prepared, despite their importance.

4. It was also found that the enterprises in question gave comparative figures for only two periods, the present and the preceding year. However, this is not very sound from a time-series analysis point of view, because such a short period may not reveal trends or may have been distorted by individual events.

5. The use of accounting techniques for the purposes of planning and control is limited. This was attributed to the weakness of the internal control system and the cost accounting system, as well as the shortage of accounting manpower.

6. The current accounting systems of these enterprises provide very little information relevant to the construction of national accounts. This was attributed to the absence of statutory requirements, the nature of the current accounting systems of these enterprises, and the lack of awareness of the national accounts' needs.

7. Very few enterprises disclose non-financial information such as employees' welfare, donations for social causes, encouragement of use of Saudi employees, health and safety protection, and pollution control. Although these enterprises, when advertising for new accounting personal, state that "priority is given to Saudi nationals", they impose very high conditions which

would be unlikely to be met by new Saudi accounting graduates.

Accordingly, government action is urgently needed to introduce greater uniformity in the classification, recording and selection of measurement methods in practice. Such action would undoubtedly improve both the quantity and quality of accounting information contained in the financial reports prepared by these enterprises.

Furthermore, given the absence of statutory requirements in Saudi Arabia, now is perhaps the appropriate time to study the possibility of linking published financial reports with national accounts, so that the information produced by the former can become a component of the information input to the latter.

CHAPTER 7

GOVERNMENT ACCOUNTING IN SAUDI ARABIA

7.1 Introduction

"Despite its long and continuous history government accounting remains academically and professionally a neglected area" (Briston, 1981, p.438).

Both developed and developing countries carry out a wide range of services from health and education to security and defence for their citizens, through public organisations. These services involve huge expenditure. For example, between 1970 and 1980, government expenditure in Saudi Arabia on such services rose from SR 6 billion to SR 283 billion (Achievements of the Development Plans, 1970-87, P.2). This vast increase was necessary to meet the requirements of development projects, including the construction of roads, schools, airports, hospitals and housing schemes.

The vast size of government expenditure and the complexity of financial transactions demand a sound government accounting system. The purpose of this chapter is to examine the main features of the government accounting system in Saudi Arabia in order to determine whether the system has developed sufficiently to keep pace with the rapid economic development during the past two decades.

Because of its importance, the state budget will be discussed first. Its development, processes, control and classifications will all be dealt with in detail. This

will be followed by a discussion of the closure of accounts and preparation of the state's final accounts. The General Auditing Bureau (GAB), the main government institution in control of public funds, is also discussed. An evaluation of the government accounting system as a whole will be made in the last section.

7.2 The Development of the State General Budget in Saudi Arabia

The general budget in Saudi Arabia has developed alongside the development of the financial system of the country as a whole. Soon after the founder of Saudi Arabia, King Abdul Aziz Al-Saud, entered Makkah and gained control of the Hejas (western region), he created the first financial administration office under the direction of Al-Sharif, Sharf Redia in 1345H (1925), who was replaced by Sheikh Abdullah Al-Sulaiman in 1346H (1926). A year later, the financial administration office was transferred to the Agency-general for Finance and remained under the direction of Al-Sulaiman. The agency was given the responsibility to organise the general revenues and expenditure of the state. This was regarded as the first legal framework of the general budget in Saudi Arabia (Al-Saloum, 1986, p.296).

The first official State budget in Saudi Arabia was published in 1351H (1931), for the financial year 1350/51H (1931) which commenced on the first day of Shaban and finished on the last day of Rajab¹ (Ibid).

¹ Shaban and Rajab are the eighth and seventh month of the Hijra Calendar.

The size of the first budget was small. It contained only the expenditure side, which totalled five million Saudi Riyals; there was no figure on the revenue side (Asfuor, 1973, p.3).

In 1351H (1931) the Agency-general of Finance was transformed into the Ministry of Finance and consequently Sheikh Al-Sulaiman became the first Saudi Finance Minister. This was followed by the issue of a Ministry bylaw which explained its functions and responsibilities (Al-Saloum, 1986, p.297). The function of the Ministry of Finance has been defined as to manage all Government finance, including the budgeting and expenditure of all ministries and government agencies, and to control national economic growth.

The first instructions concerning the state accounts were issued by royal decree no. 5/1/3/203 dated 2/2/1374H (1954). This decree also changed the beginning of the state's fiscal year. The beginning and the end of the Hegira year were chosen as a basis of the fiscal year. Accordingly, the new fiscal year started on the first day of Muharram and ended on the last day of Dhul-Hajjah². In 1376H. (1956), the instructions for budget and accounts were published. These instructions, which are still in force, were an important step towards the development of the government accounting system in Saudi Arabia at that time (Ibid).

² Muharram and Dhul-Hijjah are the first and twelfth month of the Hejra Calender.

The beginning of the fiscal year was changed for the second time by royal decree No. 8 dated 1378H (1958). Under this decree the financial year started on the first day of Rajab and ended in the last day of Jomad thani³. The reason given for the change was that the previous date corresponded to the hajj (pilgrimage) season in which most ministries and government agencies were engaged in the pilgrim operations and consequently unable to prepare and submit their budgets on time (Ibid., p.298).

7.2.1 Budget Reform Programme

The reform of the financial system of Saudi Arabia in general and the budget in particular came as a result of the increase in the country's revenues during the second half of this century. The reform programme was initiated by a number of experts from the United States of America. The American economist Ramon Knauerhase (1975, p.238) who served as an expert in Saudi Arabia during the 1950s has this to say about the reform programme:

"By the early 1950s the government realized that the increasing oil revenues provided a unique opportunity to accelerate the country's economic development. To achieve that end it was decided in the summer of 1951 to invite a group of U.S. financial experts into the country. The U.S. government formed a group of experts for this purpose and send them to Saudi Arabia under the auspices of the Point Four Program. In October 1952 the main aspects of the reform program recommended by the experts were implemented."

³ Rajab and Jumad thani are the seventh and sixth month of the Hejra Calendar.

The first phase of the reform programme resulted in the establishment of a modified central bank called the Saudi Arabian Monetary Agency (SAMA) with the following functions (Ibid):

1. Stabilizing the internal and external values of the Riyal;
2. Holding the country's monetary reserves;
3. Selling gold and silver for the government;
4. Assisting the Ministry of Finance and National Economy in holding the government's expenditures within the annual budget; and
5. Regulating the commercial banks.

The remaining phases of the reform programme were implemented later, including the establishment of the Institute of Public Administration (IPA) in 1962 to improve the quality of civil service employees, and the Higher Committee for Administrative Reform (HCAR) in 1963 to ensure that all the necessary steps to facilitate the reform were taken (Ibid., p.320).

As for the development of the state budget in particular, the Ministry of Finance and National Economy contracted for the Ford Foundation to offer it technical and consultative assistance.

In 1385H (1965) the Ford Foundation submitted its report. One of the main recommendations was that the Planning Programming Budgeting System (PPBS) should be adopted in Saudi Arabia. The PPBS:

"... seeks to establish goals and objectives for each major area of an organization's operations. Priorities are determined for the attainment of goals and objectives by executive management and conveyed to operational managers who, in turn, develop possible alternative programmes. The total cost of each programme is related to the total benefits that would be derived from the programme to determine the efficiency of the programme. The most effective and efficient programmes are selected, integrated into a comprehensive programme, and implemented" (Glynn 1987, p.263).

The PPBS was adopted by two ministries in Saudi Arabia, Health and Education (Al-Saloum 1986, p.302). However, it met with many difficulties, and so was never fully implemented.

7.2.2 Reasons for Failure of PPBS

Asfour (1977, p.44) gave four main reasons for the failure to implement the PPBS in Saudi Arabia. These were: (1) the idea of the programme was unclear to many government authorities; (2) the General Administration of Budget did not take decisive action concerning the implementation of the programme. It was left to the individual ministry to decide whether the programme format was applicable for its budget or not; (3) the practice of the programme was new to all ministries and uncertainty was a barrier to its successful implementation; (4) it was felt by most officials that if the system had failed in its country of origin (i.e. United States), it had little chance of success in Saudi Arabia.

A further reason was the absence of effectiveness auditing. As Briston (1986, p.19) argues:

"Unless a full system of effectiveness auditing is established, then there is no way that PPBS can work, for it is incompatible with traditional compliance auditing. Indeed, it could be argued that effectiveness auditing is utterly pointless without a PPBS system which has at its core the search for effectiveness, and, in the same way, PPBS will be abortive unless it is supported by effectiveness auditing."

Indeed, governmental auditing in Saudi Arabia is still confined to legal and financial compliance through detailed voucher audits with very little attention, if any at all, given to the efficiency, economy, and effectiveness of public expenditures (see sec.7.7).

Despite the difficulties encountered with the implementation of the PPBS either in Saudi Arabia or elsewhere, it is still considered the best alternative to the traditional budget approach. The programme budgeting approach should lead to better managerial planning and control because resources could be allocated more precisely to specific activities, and actual achievements could be monitored more effectively. Accordingly, it would be useful to reconsider the implementation of the system in Saudi Arabia, taking into account the change in the status of the public administration from when it first introduced in 1965 to the present. However, such a step should be preceded by the amendment of current accounting procedures and formats to comply with the requirements of the system (e.g classification of

government expenditures into programmes, activities and projects) and sound linkages between the development plan and the annual budget should be established in all government units. Also the budget officers should be trained for this purpose.

7.2.3 Recent Change of Fiscal Year in Saudi Arabia

Owing to uncertainties prevailing in the world oil market since 1985 and concomitant difficulties experienced in forecasting oil revenues, the Kingdom's budget for 1406/07H. (1986/87) was postponed for five months by the Council of Ministers' Resolution No. 144 dated 29/6/1406H (1986).

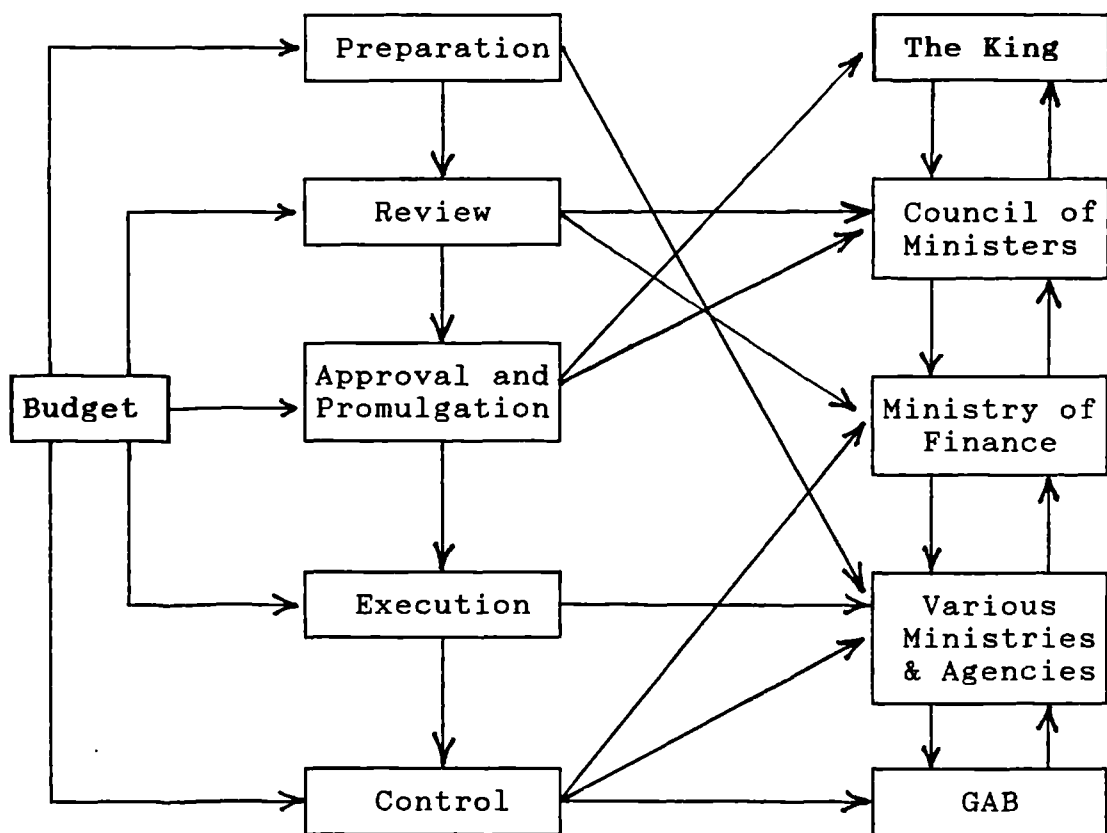
After careful consideration of the timing for oil payments and other factors related to the preparation of the budget, the Council of Ministers concluded that the Zodiac calendar was more suitable for the fiscal year than the lunar year followed so far. Accordingly, the 10th Capricorn, corresponding to the 31st of December, was stipulated to be the beginning of the Kingdom's fiscal year starting from 1407/08H (1987/88). The fiscal year 1406/07H (1986/87) was only ten months duration ending in Rabi Thani 1407.

7.3 Budget Process in Saudi Arabia

The government budget in Saudi Arabia goes through various phases: preparation, review, approval and promulgation, execution, and control. These phases constitute the formal elements of the budget calendar as

illustrated in figure 7.1. Each phase involves the active participation of several agencies and individuals. The budget process is intended to reduce conflict and to permit decisions that are acceptable to the participants. The purpose of this section is to discuss the activities taking place in each phase in more detail.

Figure 7.1
Budget Process in Saudi Arabia



7.3.1 Budget Preparation

The budget preparation begins with the circulation of what is known as "the budget call circular" sent by the Ministry of Finance and National Economy (MOFNE) to all ministries and public agencies with an independent budget, six months before the end of the current financial year. In this circular the MOFNE set forth in

general terms the instructions to be adhered to in preparing the annual budget. It includes rules concerning budget formats, methods of calculation, and the submission deadline.

Each ministry and public agency has to prepare its own budget as soon as it receives this circular and then submit it to the MOFNE by the specified date. All departments within a ministry or public agency cooperate with the help and advice of a financial representative of the MOFNE to prepare their annual budget. The preparation includes the estimation of the next year's expenditure, which is normally based on that of the previous year except where there is a new directive or financial instruction to be considered. However, any increase or decrease in expenditure must be justified in a written memorandum to be attached to the new budget.

7.3.2 Budget Review

The review phase starts after all ministries and public agencies have submitted their budgets to the MOFNE. The review phase takes place in the General Budget Department (GBD) within the MOFNE. The GBD prepares the final budget document and submits it to the Council of Ministers for further review and discussion, follows up budget execution, and recommends transfers and supplementary funds if needed.

The task of reviewing the budget is undertaken by the GBD's staff as well as representatives from the Ministry of Planning, the Civil Service Bureau, the

General Audit Bureau and the ministries and public agencies whose budgets are being reviewed. At this stage the representatives of each ministry and public agency are required to justify their requested budget. Due to the absence of specific criteria to be followed during the preparation phase, most government ministries and agencies tend to exaggerate their requirements. According to one official (interview No. 13)

"It is common to find at this phase [i.e. review] that some ministries and public agencies overestimated their requests. Thus special attention is given to such cases in order to reach a compromise solution with them in the light of budget rules and the availability of financial resources. Otherwise the matter will be forwarded to the higher authorities to take the proper action."

He further commented that public agencies, particularly during a period of economic boom, are given a lump sum to spend on their activities without specific limitation.

Indeed, even the budget review and the allocation of funds at the committee level in the MOFNE is based upon *ad hoc* procedures or what is described by one official as "jobs bargaining". This approach is normally affected by many other factors which are not economic.

7.3.3 Budget Approval and Promulgation

The GBD integrates all budgets into one document called the "State Budget" and submits it to the Council of Ministers at least one month before the beginning of the new financial year. Here the budget is further

reviewed to ensure that it is prepared in accordance with the general policy of the state, the national development plan and the government's financial law and regulations. If no amendment is needed, the budget will then be approved by the Council of Ministers. However, it may be returned to the MOFNE in the case of any amendment suggested by the Council of Ministers. If, for any reason, the budget has not been approved before the start of the new fiscal year, the budget of the previous year must be followed until the new budget is approved.

Once the budget is approved by the Council of Ministers it must be forwarded to the King for approval, after which he issues a Royal Decree promulgating the annual budget of the state for the coming year. The budget decree normally includes rules and guidelines to be followed during the execution of the budget. The following is a summary of the articles of the Royal Decree which promulgated the state budget in Saudi Arabia for the fiscal year of 1990 (Saudi Gazette, January 1, 1990, p.3):

With the help of God, most high, we, Fahad Bin Abdul Aziz Al-Saud, King of the Kingdom of Saudi Arabia:

After referring to Article 33 and 37 of the Council of Ministers Regulation issued by Royal Decree No. 38 dated 22/10/1377H [1957]; and after referring to explanatory information relating to revenues and expenditure of state for fiscal year 1410-1411H.[1990]; and after referring to the Council of Ministers' Resolution No. 94 dated 3/6/1410H, decree the following:

First: (A) The State revenues for fiscal year 1410-1411H [1990] shall be estimated at SR 118 billion. (B)

The state expenditure ... shall be authorized at SR 143 billion.

Second: For the purpose of increasing the general State budget to balance the development expenditure authorized in the budget, the Ministry of Finance and National Economy is authorised to borrow a sum not exceeding SR 25 billion gradually during the fiscal year 1410-1411H through the issue of treasury bonds in Saudi Riyals at varying maturity dates.

Third: Revenues will be effected in accordance with financial regulations and paid in full to the Saudi Monetary Agency and its branches at the account of the Ministry of Finance and National Economy.

Fourth: Expenditure will be spent according to the budget and instructions pertaining thereto.

Fifth: (A) Inter-transference among sections and subsections of the budget shall be on the approval of the Prime Minister on the basis of a joint report by the Minister or the head of the department concerned with independent budget, and the Minister of finance and National Economy. (B) Inter-transference between items of the first and second sections shall be effected by a decision from the Minister or head of the department concerned with independent budget provided that transferred amounts shall not be more than half the original amount allocated to it in the budget, excluding the salary section where transference may not be made except in accordance with (A) above.

Sixth: No allocation may be used except for its authorised purpose and no payment order may be issued over what is allocated and no expenditure may be incurred that is not provided for in the budget.

Seventh: It is not permitted to adopt any decision or sign any contract that might lead to a commitment in the next fiscal year, excluding the following: (A) Contracts which are characterized by continued implementation and periodic execution, such as rent, labour, services and food provision contracts etc. (B) Import contracts whose costs have been approved in Chapter II, on condition that their value should not exceed the allocations approved in the budget, and that the duration of the execution of the contract should not

go beyond the end of the fiscal year. (C) Project contracts, which could not be split, on condition that their value be within the approved allocation of each project.

Eighth: If it appears during the current fiscal year that there are financial obligations originating in previous years and whose amounts exceed allocations, it is deemed necessary to refer the matter to the Council of Ministers if the excess is the result of an unjustifiable act. If otherwise the Minister of Finance and National Economy is authorized to issue an order for payment of these amounts from the allocations of the current fiscal year.

Ninth: It is not permitted to appoint or promote employees except in jobs mentioned in this budget and according to conditions and classifications stipulated in effective regulations.

Tenth: With the exception of the appointment of Ministers, the creation of new jobs not included in this budget is not allowed save for jobs created according to the conditions included in the temporary jobs regulations. It is not permitted to amend the appointments allowed in this budget through promotion, though it could be changed by demotion on a decision by the President of the Civil Service Bureau made on the basis of a recommendation by a committee consisting of representatives of the Ministry of Finance and National Economy, the Civil Service Bureau and the organisation concerned.

Eleventh: The implementation of administrative structures of each department included in this budget is approved. No amendment is allowed unless it is approved by the Higher Committee of Administrative Reform. It is permissible to amend job titles on a decision by the president of the Civil Service Bureau made on the basis of a recommendation by a committee consisting of representatives of the Ministry of Finance and National Economy, the Civil Service Bureau and the organisation concerned.

Twelfth: The Minister of Finance and National Economy is authorized to issue instructions necessary to implement this budget within the framework of rules stipulated in this decree.

Thirteenth: The Deputy Prime Minister and Ministers, each in his field of specialization, are instructed to implement this decree.

7.3.4 Budget Execution

Once the budget is finally promulgated by the King, the responsibility for implementing it rests with the Ministry of Finance and National Economy. Within approximately fifteen days from the promulgation date, the MOFNE sends to each Ministry and public agency with an independent budget its approved budget together with a copy of the Royal Decree which includes instructions on budget execution. They then begin to implement their budgets within this framework. For example, they may appoint new staff, promote old staff, if they meet the criteria for such promotion, purchase goods and services and so on.

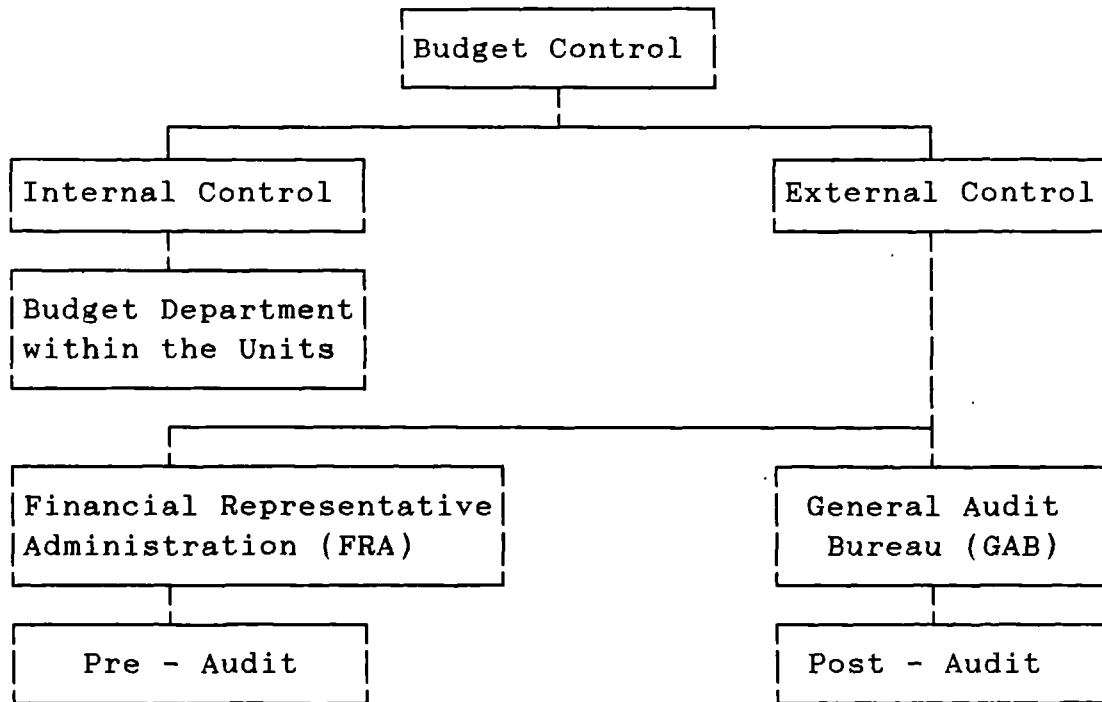
7.3.5 Budget Control

This is the final phase in the budget process, though in effect it starts simultaneously with the budget execution phase. The aim of budgetary control is to ensure that actual expenditure is in line with the budgeted amounts and that the objectives and levels of activity envisaged in the budget are achieved.

In the Saudi Arabian financial system, there is both an internal and an external control on the budget execution. The former takes place within the government units themselves, while the latter is exercised by the Financial Representative Administration (FRA) which

carries out pre-audit and by the General Audit Bureau (GAB) which carries out post-audit (see figure 7.2).

Figure 7.2
Budget Control in Saudi Arabia



7.3.5.1 Internal Control

Each of the ministries and agencies has an internal control unit responsible for monitoring its own budget in accordance with the Royal Decree instructions, government laws and regulations, and organisations' bylaws pertaining to financial affairs. In effect these units are usually attached to the financial department of the ministry or agency and report directly to the financial manager of the organisation in question.

7.3.5.2 External Control

External control of budget execution is exercised by the FRA and GAB. The role of FRA is explained below, while the GAB and its functions will be dealt with in a separate section (see sec. 7.7) because it is a totally independent control body reporting directly to the Council of Ministers and the King.

7.3.5.2.1 Financial Representative Administrative (FRA)

The FRA is a division established within the Ministry of Finance and National Economy by Royal Decree No. M/85 dated 1380H (1960). Its main function is to exercise a prepayment audit in every Ministry and public agency with an independent budget.

In order to carry out its task, the FRA has an officer in each government department and public agency appointed by the Minister of Finance and National Economy called "Financial Representative". In the case of educational institutions this officer is appointed by the President of the institution (interview No. 8). In both cases the responsibility of this officer are as follows (FRA's Code, pp.7-9):

- 1) To monitor the general budget execution in accordance with the Royal Decree instructions, paying particular attention to constraints on payments to ensure that they are made within the approved expenditures specified for each chapter.

- 2) To audit transaction vouchers before payment to ensure their legality and that all necessary procedures

have been completed; also to ensure that payments are not made twice.

3) To examine loans and deposit-trusts quarterly to ensure that no fund pertaining to these accounts remains unpaid without reasonable justification.

4) To supervise entries in the accounting records, closing accounts, preparing monthly accounts and dispatching them to both MOFNE and GAB at the specified date in order to facilitate the preparation of the State's Final Accounts.

5) To supervise the filing of all documents after payment to ensure that they are properly kept and ready for the GAB inspection at any time.

6) To assist the government unit in discussing its new budget allocation before submission to the MOFNE.

7) To assist the government unit in the interpretation of laws and instructions pertaining to financial affairs with consultation with the MOFNE if necessary.

8) To study the financial status of the government unit under his supervision, to prepare a report thereon each three months, and notify each of MOFNE, GAB and the government unit concerned of the conclusions of the report.

9) To supervise warehouse records to ensure that they are properly kept and to observe inventory transactions and notify each of MOFNE and GAB of his observations in this respect.

10) To participate in committees formed for the purpose of transfer of funds among budget items.

11) To participate in bids committees formed to discuss tenders for new projects in the government unit.

12) To participate in committees formed to investigate losses of state property.

It is clear from the above that the role of Financial Representative is predominantly devoted to legal aspects. For example, no mention is made in the FAR code of ensuring that government units make efficient use of the funds allocated to them in the general budget.

7.4 Budget Classification in Saudi Arabia

There are several ways in which budgets can be classified, for example, economic, administrative, functional, by object, and geographical. Detailed study of these classifications and their advantages and disadvantages is beyond the scope of this study.

The annual budget in Saudi Arabia is based upon the traditional approach or what is known as the "Line-item" budgeting system. Accordingly, the budget is classified into two main sides, namely, expenditures and revenues. This can be illustrated by discussing the various items of budget expenditures and revenues as they appear in the general budget of the state.

7.4.1 Expenditure

Government expenditures in Saudi Arabia are mainly determined by total government proceeds, the most important component of which is oil revenue. The total government expenditure is contained in four main chapters:

Chapter I contains salaries and allowances, including civil and military employees, fixed salaries, wages of daily workers, etc.

Chapter II deals with general recurrent expenses, including travel and transport expenses, stationery and printing supplies, maintenance of airports, roads and government installations, etc.

Chapter III includes all aids and subsidies paid by the government for various groups such as athletic clubs, electric companies and other social organisations.

Chapter IV covers the non-recurring items which are described as projects associated with the development of the social and physical infrastructure. For example the following items are listed under this chapter:

1. Purchase of land and building.
2. Building construction.
3. Other construction.
4. Machinery and equipment.
5. Transport equipment.

For control purposes, each of the above chapters has been given a special code. For example, chapter I is given the code number 100 and chapters II, III, and IV

are given the code numbers 200, 300 and 400 respectively. In addition, items included in each chapter are coded accordingly. Table 7.1 shows how the code for an individual items appears in chapter I of the annual budget.

Table 7.1
The Main Accounts of Chapter I

Account name	Code No.
Civilian Salaries	101
Military Salaries	102
Fixed Salaries	103
Wages of daily workers	104
Allowance	105
Compensation	106
Travel Allowance	107

For any expenditure to be made, it has to be specified in the above four chapters and no fund may be transferred from one chapter to another without authorization (interview No. 20). Usually, the Royal Decree governs the authority to transfer funds and sets the procedures and guidelines for the kind of accounts where transfer may be allowable. However, transferring funds from chapter four to any of the other chapters is not allowed in any circumstances.

In addition to the classification of expenditures into recurring and non-recurring, they are also classified by function into groups such as human resource development; agriculture and water; health and social development; transport and communications; municipal services; industry, electricity and housing; defence and security services; and domestic subsidies. Table 7.2

shows the total amount allocated to each of these sectors as it appears in the budget [for the fiscal year 1410/11H (1990)].

Table 7.2
Budget allocation for 1410/11H (1990)
by major economic sectors

Major Economic Sectors	Millions SR
Human Resource Development	26.191
Agriculture and Water	6.890
Health and Social Development	11.791
Transport and Communications	9.228
Municipal Services	6.890
Industry, Electricity and Housing	4.795
Defence and Security Sectors	51.898
Domestic Subsidies	7.183

Source: Saudi Gazette, January 1, 1990, p.1

Each of the above sectors consists of various government ministries, agencies and institutions. For example, human resource development consists of the following:

1. Ministry of Education.
2. General Presidency for Girls' Education.
 - Girls' Colleges.
3. Ministry of Higher Education.
 - King Saud University
 - King Abdul Aziz University
 - King Fahad University
 - King Faisal University
 - Imam Mohammad Bin Saud Islamic University
 - Islamic University - Madina
 - Umm Al-Qura University.
4. Ministry of Labour and Social Affairs.
5. General Organization for Technical Education and Vocational Training (GOTEVT).
6. Civil Service Bureau.
7. Manpower Council - General Secretariat.

8. King Abdul Aziz City for Science and Technology.

9. Institute of Public Administration.

7.4.2 Revenues

Despite their relative decline in recent years, sales of crude oil remain the dominant source of revenues in Saudi Arabia. However, there are several sources of non-oil related revenues:

1. Income tax imposed on non-Saudi companies and on shares owned by non-Saudis in Saudi companies.

2. Zakat imposed on Saudi companies and on shares owned by Saudis in non-Saudi companies.

3. Oil products tax which is levied on the consumption of imported oil products.

4. Customs duties imposed on other imported goods.

5. Charges for public services, such as in land and oil port and airport fees, and revenues from commercial registration.

6. Telecommunications charges.

7. Sales of documents such as government regulations, bylaws, passports and identity cards.

8. Miscellaneous.

For control purposes, each of the above sources of revenue has been given a special code. The revenue side of the budget is divided into 12 major accounts, some of which are divided into subaccounts (see table 7.3). The major classifications are oil production (account number 8,000), income tax (8,100), Pipeline fees (8,200), oil products tax (8,300), customs duties (8,400), transport

Table 7.3
Revenue Classifications, and Subaccounts

Control Account Number	Sub-account Number	Classification
8,000		<u>Oil Production</u>
	8,001	Aramco
	8,002	Jetty Oil
	8,003	AOC
8,100		<u>Income Taxes</u>
	8,101	Aramco
	8,102	Jetty Oil
	8,103	AOC
	8,104	Other Companies
	8,105	Individuals
8,200		<u>Pipeline Fees</u>
8,300		<u>Petroleum Product Tax</u>
8,400		<u>Customs Tariffs</u>
	8,401	On value
	8,402	Specified
8,500		Transportation Tax
	8,501	Railroad and Dammam port
	8,502	Vehicle licences
	8,503	Road Tax
8,600		<u>Services</u>
	8,601	General service fees
	8,602	Municipalities
	8,603	Port fees
	8,604	Airport fees
	8,605	Landing fees
	8,606	Post
	8,607	Telegram
	8,608	Telegraph
8,700		<u>Documents</u>
	8,701	Publications
	8,702	Stamps
	8,703	Drivers licences, work permits
	8,704	Residency and passports
8,800		<u>Government Sales</u>
8,900		<u>Rents</u>
	8,901	Public property rents
	8,902	Employees housing
9,000		<u>Miscellaneous</u>
	9,001	Profits
	9,002	Fines and penalties
	9,003	Other revenues
10,000		<u>Zakat</u>

Source: Knauerhase, R., 1975, p.259

tax (8,500) services (8,600), documents (8,700),
government sales (8,800), rents (8,900), miscellaneous

revenues (9,000), and Zakat (10,000) [Knauerhase, R., 1975, p.258].

7.5 Closure of Accounts and Preparation of State's Final Account

7.5.1 Closure of Government Units' Accounts

The purpose of the closure accounts is to meet the requirements of appropriation audit and to provide information to the public on the status of the government finances. In the Saudi Arabian system, the Financial Instructions for Budget and Accounts set forth guidelines concerning the closure of the accounts of each accounting unit and the preparation of the state's final accounts. According to these instructions the accounts of each accounting unit are closed daily, monthly and annually as follows:

7.5.1.1 Daily Closure

At the end of each day the accounts must be closed and a trial balance prepared. This can be done by totalling the journal columns and comparing the total of the right page with that of the left page to ensure the accuracy of entry in all accounts(Para 79).

7.5.1.2 Monthly Closure

At the end of each month the accounts must be closed and an accumulated trial balance must be prepared. These trial balances include the operations in both the main and subsidiary accounts that take place during the month in question. After closure of each month's accounts, the

totals should be posted to the next month's accounts together with supporting tables, after being signed by the financial manager or head of accounts and the president of the agency concerned (Para 80-83).

7.5.1.3 Annual Closure

At the end of each financial year, the accounts of all government units must be closed and final trial balances must be prepared. These include all accounting adjustments related to the financial year for both main and subsidiary accounts. All ministries and agencies are required to submit their final accounts to the Ministry of Finance and National Economy on a specified date (Para.85).

The final accounts of each government unit must be signed by its president, the head of the accounts department, and the financial representative of the unit. Three copies are prepared, the first being sent to the Ministry of Finance and National Economy, the second to the General Audit Bureau and the third remaining with the government unit.

All of the documents pertaining to the revenue and expenditure (e.g. receipts and payment vouchers) of the unit must be enclosed with the final accounts. In addition, the final account must be accompanied by an explanatory memorandum indicating any changes occurring during the financial year in question, for example, justification for any increase or decrease in revenue and

expenditure, transfer of funds from one chapter to another or among the items within the chapter (Ibid.).

7.5.2 Preparation of the Final Accounts of the State

The preparation of the final accounts of the state is the responsibility of the Ministry of Finance and National Economy, Department of General Accounts (interview No. 3). These accounts are prepared from the final accounts of the various government ministries and agencies, and must be submitted by the Minister of Finance and National Economy to the Council of Ministers within four months from the end of the financial year. A copy should also be sent to the General Auditing Bureau to enable it to prepare and submit its annual report according to the provisions of article 8 (c) of the Council of Ministers Code (Para 81).

7.5.3 Problems with the Final Accounts of the State

The Ministry of Finance and National Economy suffers from many problems which hamper the prompt preparation and submission of the final accounts. According to Al-Sharif and Al-Emam (1988), who both senior government officials, these problems include:

1. Lack of conformity between the current accounts kept in the Ministry of Finance and National Economy's books with the current accounts in the books of the ministries at the end of the financial year. This is due to the fact that these ministries are not reconciling their current accounts to that of Ministry of Finance and

National Economy at the end of each month and notifying the result of the reconciliation.

2. In the case of establishments allowed to open accounts with SAMA, it is sometimes the case that at the end of the financial year, the accounts kept by these establishments do not tally with those of SAMA itself, causing delay in preparing the final accounts of the establishments, and hence of the State.

3. Overstatement of trust and deposit accounts because they are not paid up to date in accordance with the financial instructions.

4. Confusion of loan accounts in some ministries as a result of failure to apply a proper accounting system.

5. Weakness in the technical ability of those dealing with financial affairs in the ministries and public agencies as well as staff shortages, which results in many errors.

7.6 Bases of Government Accounting System in Saudi Arabia

In practice there are three bases of accounting namely: cash, accrual, and obligation base.

Cash basis recognizes only cash inflows and cash outflows. In other word, only expenditures actually paid and revenues actually accumulated during a specific accounting period are included in the final accounts. Thus the cash basis ignores accrued items.

Accrual basis recognizes transactions when they occur, regardless of when cash is paid or accumulated. Thus the results of the final accounts include all

expenditures incurred during the accounting period, regardless whether they were paid, and all revenues earned during the same period, regardless of whether they were received.

Obligation basis (known also as the commitment basis) recognizes transactions when the organisation is committed to them. Thus, the transaction is not recognized when cash is paid or received, nor when an invoice is received or issued, but at the earlier point when orders are issued or received.

The Government accounting system in Saudi Arabia adheres to the cash basis (interview No. 3), which is simple and easy to apply. However, it is not problem-free. For example, it is not entirely relevant for making decisions concerning efficiency and effectiveness, both within and outside government (Briston, 1981, p.459).

7.7 General Audit Bureau (GAB)

7.7.1 Historical Perspective

The GAB goes back to the early 1950s, when the first code concerning the organisation of the Council of Ministers Bureau was issued. The code states that the Council of Ministers Bureau shall consist of the following sections:

1. General Secretariat
2. Monitoring of the Accounts of the State
3. Technical Experts
4. Grievances

The Monitoring of the Accounts of the State section was the main body responsible for auditing state accounts, and was the former of the GAB.

The code also specified the functions and responsibilities of the state auditing section as including auditing the accounts of all ministries and government units; ensuring the accurate recording of revenues and expenses and that they are in accordance with the approved allocations included in the general budget.

Although the Auditing of State Accounts was a section of the Council of Ministers Bureau, it has been given full independence, since the code stated that the head of this section and his deputy shall be appointed by Royal Decree and shall be responsible to the King; and that its budget shall be discussed and approved without reference to the General Secretariat of the Council of Ministers (Abu-hamed and Frhood, 1985, p.19).

In 1377H (1957) the executive bylaws of the Auditing of the State Accounts section were issued. These explains its internal classification and work instructions. In the same year the current Council of Ministers code was issued and the name of the audit section was changed to its present name (i.e General Audit Bureau).

Up to the 1391H (1971) the operations of the GAB were governed by various articles found within the Council of Ministers code. The first law governing the GAB operations was introduced by Royal Decree No. 9 dated

11/2/1391H (1971). This was followed by Royal Decree No 18835/35 dated 19/2/1392H (1972) which approved the executive bylaws of the GAB.

Finally, in 1978 Royal Decree no. 390 dated 13/4/1398H (1978) was issued to extend the audit of the GAB to include "any private establishment or company where the state shares in its capital or grants it minimum profits."

7.7.2 Organisation and Staffing

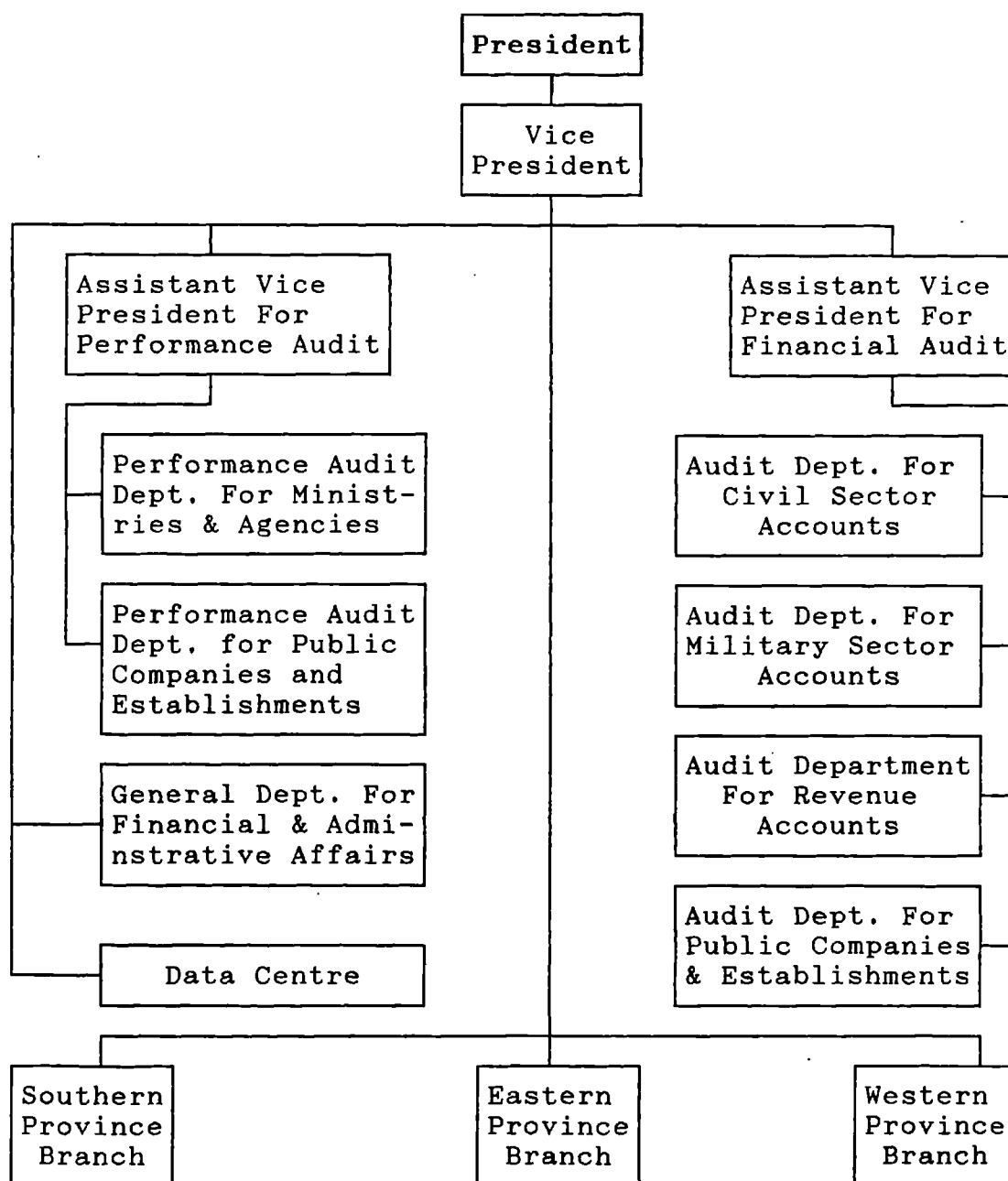
The internal organisation chart of the GAB is shown in figure 7.3. It consists of a president, vice president, two assistant vice presidents (one for financial audit and the other for performance audit), and a number of auditors (technical staff).⁴

The president and vice president of the GAB are appointed by Royal Decree. The President is given ministerial rank and reports directly to the King (Arts. 2-3). Nothing is said in the GAB's code about the two assistant vice presidents, for these two positions were created very recently. However, such positions are usually appointed by resolution of the Council of Ministers upon the recommendation of the Minister of the Ministry concerned (the president in the case of GAB). The rest of GAB's staff is appointed similarly to those in other government Ministries and Agencies. Their salaries, allowances, promotion, resignation and

⁴ As at the end of December 1989, the number of staff working in the GAB headquarters and its branches totalled around 500 (interview No. 14).

retirement are all governed by the civil service code (Art. 6). Thus there are no special financial incentives or remuneration for the AGB's technical personnel. The

Figure 7.3
The General Audit Bureau Organisation Chart



Source: Obtained by the author from the GAB Headquarters, Riyadh. (Author's Translation)

size of the technical staff is determined by the president of the GAB, according to the amount of work and the constraints of the GAB budget (interview No. 14).

7.7.3 Functions and Responsibilities

The functions and responsibilities of the GAB are set out in articles 7 and 8 of its code. For example, article 7 states that the GAB is responsible for the post audit of all government revenues and expenditures, and control of all state resources from the point of view of proper utilisation and the safeguarding of such resources. Article 8 provides more details of the functions of the GAB:

1. To verify that all state revenues, debts, goods and services have been received according to the law; and to ensure that all state expenditures have been made according to the budget rules, and financial laws and instructions.

2. To verify that all state properties are used for the purpose specified; and to ensure that government agencies can guarantee the safety and good usage of these properties. Also, to guarantee there will be no misuse of them.

3. To verify that all government departments and agencies under the supervision of the GAB apply the financial laws and instructions, and that there is no misconduct in their application.

4. To monitor the current financial laws and instructions applied in the public administration and to

verify their appropriateness to the Kingdom's development objectives; also to comment on inadequate laws and instructions by modifying them and submitting the necessary proposal to improve them or cancel them altogether.

7.7.4 Scope and Extent of the GAB Audit

The audits conducted by the GAB cover the following organisations (Art. 9):

1. All government ministries, departments, and their branches;

2. Municipalities and administrations of water supply;

3. Public establishments and other agencies which have an independent budget and receive part of the state's funds, either in the form of subsidies or for investment;

4. All private organisations and companies to which the government subscribes or makes grants or guarantees minimum profits;

5. All entities which become subject to the GAB's audit either by Prime Minister's (the King) order or by the Council of Ministers' resolution.

According to the code (Art.10), all the above organisations are required to submit their financial statements and other related documents to enable the GAB to exercise its duties and to provide all facilities required for the GAB's staff to perform their work in

accordance with the executive bylaws issued for this purpose.

7.7.5 Reporting

The president of the GAB is required to prepare an annual report and to submit it before the last day of the ninth month of the following financial year. The report should include the following (Art.20):

1. Evaluation of the financial management of the state in general through the last fiscal year;

2. Evaluation of the financial management of each department and agency under its supervision through the last fiscal year;

3. Statement on the final accounts of the state for the preceding financial year. Also, if the Ministry of Finance and National Economy has not submitted these accounts before the deadline for the annual report, the GAB's report must include the reasons for the delay and the GAB's opinion concerning the appropriate action to be followed; and

4. Summary statement about the operations of the GAB during the preceding fiscal year.

The circulation of the above report is limited to the King, Council of Ministers, and Ministry of Finance and National Economy (Art.21). However, during the financial year the president of the GAB may submit other reports either generally or concerning specific cases (Art. 22).

7.8 Government Accounting System in Saudi Arabia: An Evaluation

It would seem that the government accounting system in Saudi Arabia has not developed sufficiently to keep pace with the rapid economic development and the increasing complexity of financial transactions in the public sector. The government accounting guidelines and the system of classification of accounts which were established in 1956 are still used today, with very little amendment. This view was expressed by a government official interviewed by the author. He stated:

"Our accounting system was originally established in 1376H [1956]. As you know at that time the number of government ministries and agencies was small and consequently the nature of government transactions was simple. Meanwhile, the Ministry of Finance and National Economy alone was in charge of all government financial affairs including collection of revenues and payment of expenses; and the accounting system was organized on this basis. In contrast, today each government ministry and agency is responsible for collecting its revenues and paying its expenditures." (interview No. 3).

The government accounting systems, procedures, format and classifications are lengthy and complex. For example, payment vouchers have to go through various departments, be checked, and rechecked, and the signatures of various officials have to be obtained before the amount is finally paid. These long procedures and their excessive rigidity have undoubtedly hampered the development of the accounting system.

Furthermore, the state budget has to go through many phases before it is finally approved and executed. The budget is still a traditional or "line-item" budget, which includes certain economic functional classifications, without further useful breakdown and evaluation into programmes, activities and projects. This type of budgeting is simply a system for allocating particular kinds of inputs, which are not related in any way to the intended outputs, let alone the outcomes. Nor does it enable auditors to conduct any other audit, apart from financial and compliance audit. The initial effort to improve the budget procedures by introducing performance budgeting system has encountered many difficulties.

As far as accountability is concerned, there are serious deficiencies. For example, the role of both the FRA and GAB is limited to pre- and post-control voucher audits of governmental transactions respectively. Such audits are basically concerned with the legality of transactions, to determine whether transactions are properly conducted, in accordance with applicable laws and regulations. As indicated above, when GAB discovers an error or a financial deviation, it notifies the authority concerned requiring it to correct the matter quickly; otherwise the error is noted by the GAB to the Council of Ministers and the King. No attention is given, however, to any type of economic audit or value for money audit.

Although the organisation chart of the GAB (see figure 7.3), which has been approved by the Higher Committee of Administrative Reform (HCAR)⁵, includes a section for performance audit, it has yet to operate in its full capacity, since the GAB currently suffers from shortages of staff, both in quality and quantity. In any case the current budget classifications and the use of the basis are not helpful to the conduct of performance audit.

In order to overcome the above shortcomings and improve the government accounting system, the audit scope should be expanded to include measurements of the efficiency, economy, and effectiveness of public expenditure.

7.9 Summary and Conclusion

The purpose of this chapter has been to examine the main features of the government accounting system in Saudi Arabia. The focus has been on the development of the general state budget, which is the main component of the system. Its process, control and classification were all discussed. Closure of accounts and preparation of the final accounts; accounting basis; the GAB, its organisation and staffing, function and responsibilities,

⁵ The HCAR was established as part of the reform programme mentioned earlier (see sec. 7.2.1). The president of the HCAR is the King; the vice president is the Second Deputy Prime Minister and Minister of Defence and Civil Aviation; and the membership consists of five Ministers, including the Minister of Finance and National Economy, the Minister of Planning, two Ministers of State, and the President of the Civil Service Bureau. It has power equal to that of the Council of Ministers.

scope and extent of audit were also examined. The system as a whole was evaluated in the last section.

It was found that the system is out of date, taking into account the size of the government sectors and the complexity of government transactions today, compared with when the system was first established in 1956. Accordingly, action is urgently needed to amend the system, its formats, classifications and procedures in order to provide more reliable, accurate and timely information. Perhaps the most urgent needs are to cut down the lengthy procedures currently applied in the public sector, to unify accounting principles and procedures among the government units, and to encourage all government units to use electronic data processing to handle their transactions.

CHAPTER 8

NATIONAL ACCOUNTING IN SAUDI ARABIA

8.1 Introduction

National accounting data for a series of years are essential for an analysis of the growth of an economy, for forecasting and planning, and for the study of economic structure.

There are various alternative names for the term "National Accounting", for example, macro accounting, social accounting, economic accounting, and national economic accounting. However, despite these differences in the prevailing terminologies, they all deal with economic activities at aggregate level. As Enthoven (1973, p.65) states:

"While micro accounting deals with a single micro entity (such as the business enterprise), social accounting covers similarly the economic position, activities and measurement of efficiency of more macro entities in a community, which entities - showing costs and benefits at aggregate levels - may be a whole industry, a sector, or the economy as a whole."

The purpose of this chapter is to examine the national accounts in Saudi Arabia. The discussion will be focused on the development of national accounts in Saudi Arabia, classification of the national economy, type of national accounts currently prepared, nature and sources of data, users of national accounts in Saudi Arabia, major problems encountered in their construction, and how these problems can be alleviated.

It is not, however, the purpose of this chapter to discuss the statistical methodology involved in constructing national accounts. Nevertheless, before examining the national accounts in Saudi Arabia it is useful to explain the development and objectives of national accounts in general, to serve as an introductory section to this chapter.

8.2 Brief Background to National Accounts

8.2.1 The Evolution of National Accounts

Although national accounts are a relatively new area of accounting, their concept was first formulated in the seventeenth century by Sir William Petty in England.¹ Petty aimed, among other things, to establish the effect of the industrial revolution and the external wars fought by the British upon the economic and defence ability of England (Studenski, 1958, pp.27-28).

At about the same time, Boisguillebert and Vauban were engaged in a similar attempt in France. Their main purpose was to use national income data in order to reform the French tax system (Ibid. pp.52-60).

Le Quesnay, also French, designed what was known as a "Tableau-Economique". His work was considered very important in the development of national accounts (Ibid. pp.61-65).

The United States saw similar attempts to those occurring in England and France, though rather later. The

¹ For a comprehensive study of this subject, see Paul Studenski, the Income of Nations, New York, 1958, particularly part one: History

first national income estimates in the US were made by George Tucker in 1843. However, no other American statistician or economist did any work in this field until 1896, when Charles Spahr published an estimate of American national income for that year. According to Studenski, the reasons for this lengthy lapse of interest are not easy to determine (Ibid. pp.129-132).

The efforts of these earlier scholars laid down the main framework for the development of national accounting. However, it was not until the beginning of the Second World War that a start was made on bringing the estimates of national income and related totals together in the framework of a system. For example, in 1944, national income experts from United Kingdom, Canada, and the United States met in Washington. Their main purpose was to establish a uniform procedure to be followed when preparing national income accounts, so as to make them more comparable and useful to their respective governments (Ibid., p.154).

The early efforts toward the development of national accounting thus mainly came from economists and statisticians, without the involvement of accountants. This was pointed out by Powelson (1955, p.651):

"Although social accounting applies the same double-entry rules as business accounting, and makes use of accounting techniques long accepted in the business world, it has been largely ignored by accounting professors in American universities."

Finally, the role of the United Nations in the development of national accounts must not be ignored. For example, the UN established a special agency to help member countries to use national accounting data for the purpose of development planning. Meanwhile, it has prepared and published a number of guidelines and provided advice in this field for its members (e.g. UN System of National Accounts of 1953 and 1968).

8.2.2 The Objectives of National Accounts

In the past, the national accounts were designed to compare the wealth and power of individuals in terms of their annual income, rather than to provide information relevant to the economy as a whole. As Regulase and Regulase (1956, p.7) state:

"In its early stages national income accounting was not designed as a method of presenting information relevant to general economic problems. ... Their primary concern was the building up of a series of aggregates for successive time periods to show the total income of all individuals in a particular country. ... At this stage in the development of national income, however, there was no explicit attempt to construct a framework of data for the economy as a whole."

Over the years, national accounts have developed to meet the requirements of economic planning, including data for the preparation of projects and of sectoral and national plans. O'Loughlin (1970, p.7) gives two main objectives for national accounts in modern times: first, to present a description of the economy in statistical

terms in the form of a pattern of accounts and tables; and secondly, to guide the use of this system of measurement for planning and policy process.

Enthoven (1973, p.66) argues that countries - and particularly developing countries - need social accounting for:

"... setting goals in quantitative terms; devising development strategies, policies, plans and budgets; making decisions (in the macro and micro economic spheres); measuring economic welfare and progress; and international comparisons and policies."

The main objective of national accounting is thus to provide useful information to be used for development planning purposes at the national level.

The chapter now turns to a discussion of the national accounts in Saudi Arabia, the material for which is based upon interviews conducted by the author with the National Accounts Section officials² in Saudi Arabia in December 1989, together with a review of various national accounts published by Central Department of Statistics.

² See chapter 1 for research methodology and Appendix C for the list of interviewees.

8.3 The Evolution of National Accounts in Saudi Arabia

The preparation of national accounts in Saudi Arabia is the responsibility of the Central Department of Statistics (CDS). The CDS was established by Royal Decree number 23 dated 7/12/1379H (1959), which also set out its functions and operating procedures. The CDS operates currently under the authority of the Ministry of Finance and National Economy (MOFNE). Its headquarters is located within the MOFNE and its internal organisation chart (see figure 8.1) consists of four main sections:

1. Statistical Section, which carries out research in various economic and social fields.

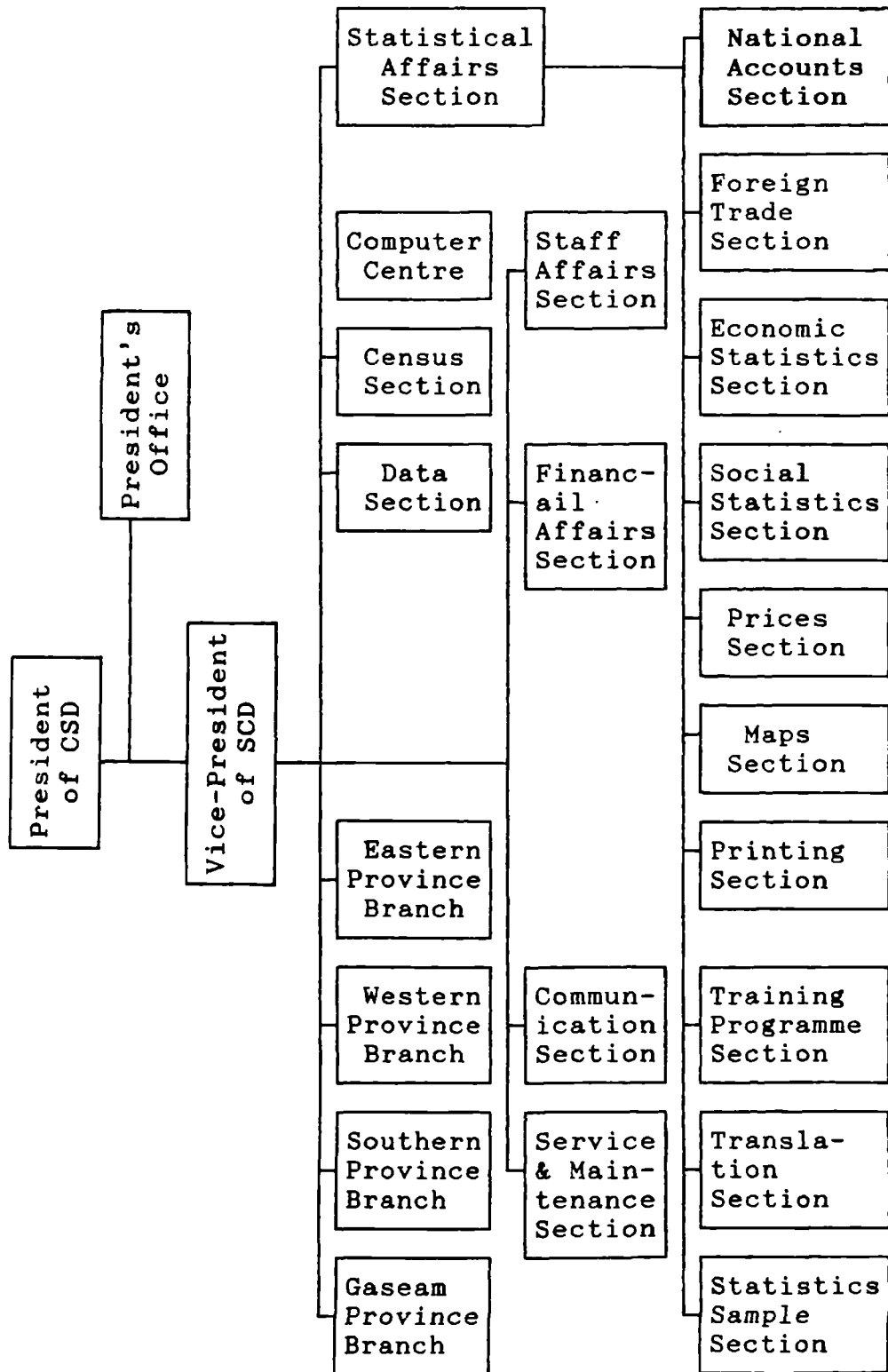
2. National Centre for Computers Section, which provides computer services for the CDS, as well as other government ministries and agencies.

3. Branches of the CDS Section. Currently there are four branches of CDS located in four different provinces, namely, eastern, western, southern, and Gaseam. The CDS also has five offices in Macca, Medina, Hofuf, Taif and Tabuk.

4. Administrative and Financial section, which is responsible for all administrative and financial affairs of the CDS and its branches.

The first set of national accounts in Saudi Arabia was published by the CDS in 1967. They were prepared in accordance with the UN old system of National Accounts. Due to the lack of data and shortage of staff, most input

Figure 8.1
The Central Statistical Department (CSD)
Organisation Chart



Source: Central Department of Statistics (CDS), Riyadh, Saudi Arabia (Author's Translation).

data had to be roughly estimated from various sources (interview No. 10).

A second set of national accounts with supporting tables was published by the CDS in 1978. They covered the period from 1968/68 to 1978/77, and also included forecasts of gross domestic product for 1977/78 for the three traditional sectors, namely: oil, private non-oil sector, and government sector. Since then, the CDS has published a series of national accounts including gross domestic product by type of economic activity in producer's values at current prices, government final consumption, gross fixed capital formation, and external transactions.³ The time required for the preparation of national accounts ranges from six to nine months, depending upon the availability of the input data required for their construction (Ibid).

8.4 Classification of National Economy in Saudi Arabia

In preparing its national accounts, Saudi Arabia follows closely the UN new System of National Accounts which was published by the United Nations in 1968 (interview No. 2). According to its authors (p. iii), the system "provides a comprehensive and detailed framework for the systematic and integrated recording of the flows and stocks of an economy. It brings together data ranging in degree of aggregation from the consolidated accounts of the nation of the old to detailed input-output and

³ Balance of Payments is currently prepared by the Saudi Arabian Monetary Agency (SAMA).

flow-of-funds tables into an articulated, coherent system."

However, due to lack of statistical data in Saudi Arabia it is not possible to implement the UN system in a comprehensive manner. Apart from the problem of statistical data, the UN new system of national accounts is not easy to operate, particularly in developing countries because of the difficulties associated with the system itself. As argued by Barkey (1975, p.361):

"It appears that there are grave difficulties in the adoption of the full system of the United Nations national accounts to those developing countries I happen to be familiar with. In addition to theoretical difficulties the system is far too complicated and ambitious, not suitable to the limited statistical resources available in the developing countries."

Indeed, the difficulties of implementing the UN system are recognized even by its own authors, who state (p. 207) that "it will take a number of the developing countries many years to build the body of statistics required to compile the standard accounts and tables of the system".

For the purpose of preparing national accounts, the national economy of Saudi Arabia is classified into four main sectors as follows (interview No. 10):

1. Producing sector.
2. Government sector.
3. Household sector.
4. External world sector

These sectors will be briefly discussed below.

8.4.1 Producing sector

This sector includes all economic units which produce goods and services for sale at a price which is normally intended to cover their cost of production, or produce these goods and services for their own use in all economic activities included in the ISIC.⁴ The following are included under this sector:

1. Boards and government non-financial producing enterprises: this includes all government economic units which produce goods and services, whether for sale at a price which covers their production cost or at a lower price as a result of government price policies, or for private use within the administration of government, taking into account that all these units are financed and managed by the government.

2. Non-Financial Joint Sector: this includes all economic units which produce goods and services for sale at a price which covers their cost of production, but whose capital is owned jointly by individuals and government companies.

3. Private non-Financial Sector: this includes all resident economic units which are owned and managed by the private sector. These units are divided into two main categories:

⁴ International Standard Industrial Classification of all Economic activities, Statistical Papers, Series M No.4 United Nation, New York, 1968.

3.1 Organised Enterprises: these include all enterprises which keep independent books and financial accounts, such as Joint Liability Partnerships, Simple Limited Partnerships, Partnerships Limited by Shares, Limited Liability Companies, and Corporations.⁵ It also includes large individual enterprises which have financial accounts separate from their owners, as well as branches of foreign companies.

3.2 Non-organised Enterprises: These include small individual enterprises which do not keep independent books and financial accounts, where it is difficult or impossible to separate their financial transactions from those of their owners.

4. Financial Sector: this includes all financial units which deal mainly with financial transactions, which both acquire financial assets and incur liabilities in the market, as well as insurance companies. Accordingly, this sector includes the Saudi Arabian Monetary Agency (SAMA), Specialized Credit Institutions (currently 6), commercial banks (currently 12) and other financial establishments.

⁵ See chapter 3, for more details about the nature of these enterprises.

8.4.2 Government Services Sector

This includes all government ministries and establishments engaged in administration, defence, health, education, and other social services, welfare and promotion of economic growth. It also includes government units specializing in providing services which have a recurrent nature, such as passports, identity cards and driving licences, though the charges for such services only cover the current administrative expenses of such units.

8.4.3 Household Sector

This sector includes all individuals and families, whether they are Saudi or non-Saudi, resident within the borders of the Kingdom of Saudi Arabia for a period of more than one year. It also includes private non-profit organisations which provide services for the household sectors, such as charities, athletics clubs and the like.

8.4.4 External World Sector

This sector represents the Kingdom's transactions with the rest of the world in respect of exports and imports and all capital financial transactions which either acquire financial assets or incur liabilities for the Kingdom with the external world.⁶

⁶ The definition of terms and classifications used in these sectors are based on A System of National Accounts, Studies in Methods, Series, No.2 Rev.3, (New York: United Nations 1968).

8.5 Nature and Sources of Data for National Accounts in Saudi Arabia

The nature and sources of data used for the preparation of national accounts depend upon the nature of the accounts to be prepared, as well as the type of economic activities. The following are the main accounts currently prepared and published by CDS (interview No. 10):

- 1) The Gross Domestic Product by Type of Economic Activity in Producers' Values at Current Prices.
- 2) Government Final Consumption.
- 3) Gross Fixed Capital Formation by Type of Capital Goods in Purchasers' Value, at Current Prices.
- 4) External Transactions.

8.5.1 The Gross Domestic Product by Type of Economic Activity in Producers' Values at Current Prices

For the purpose of computing the gross domestic product (GDP), the Saudi Arabian economy is divided into: (a) Industries and other producers except government services, and (b) Producers of government services. Each of these two divisions is further sub-divided into various activities, as illustrated in figure 8.2

Figure 8.2
Gross Domestic Product by Type of Economic Activity
in Producers' Values at Current Prices

	199X
A. Industries and Other Products except Producers of Government Services	
1. Agriculture and Fishing	XXX
2. Extraction of Crude Petroleum and Natural Gas	XXX
3. Manufacturing	XXX
4. Electricity, Gas and Water	XXX
5. Construction	XXX
6. Wholesale & Retail Trade, Restaurants & Hotels	XXX
7. Transport and Communication	XXX
8. Ownership of Dwellings	XXX
9. Community, Social & Personal Services	XXX
10 Less: Bank Service Charge*	<u>(XXX)</u>
Sub-Total	XXX
B. Producers of Government Services	
1. Public Administration and Defence	XXX
2. Other Services	XXX
Sub-Total	XXX
Total Except Import Duties	XXX
Import Duties	<u>XXX</u>
Gross Domestic Product	XXX

* Figures in this section supplied by SAMA

Source: Central Department of Statistics, Ministry of Finance and National Economy, National Accounts Section.

8.5.1.1 Industries and Other Products Except Producers of Government Services

Gross Domestic Product in this category is classified according to types of economic activity based on the ISIC as recommended in the UN system. The general method used in calculating GDP is to deduct intermediate consumption in purchasers' values from gross output in producers' values. According to the UN system of 1968, intermediate consumption is defined (p.235) as "Non-durable goods and services (commodities) used up in production, including repair and maintenance of the capital stock, research, development and prospecting, indirect outlays on financing capital formation, such as flotation costs for loans, and transfer costs involved in purchases and sales of land, intangible assets and financial claims". The gross output of industries is defined (p.234) as "The value in the market of all goods and services (commodities) produced during a period account, including work-in-progress and products for use on own account. Also includes the gross output of distributive trades which is equivalent to the gross margins, that is, the differences between the sales and purchase values of the goods sold, the insurance services charge in the case of casualty and life insurance, and the sum of the actual and imputed service charges in the case of banks and similar financial institutions."

Surveys of establishments carried out by CDS are the main sources of data for all economic activities, except the petroleum and government sectors. These surveys

provide figures of gross output, and intermediate consumption from which GDP is calculated for the following activities: other manufacturing (except petroleum refining), construction other than government-financed and oil company-financed construction, wholesale and retail trade, restaurants and hotels, storage, finance, insurance, real estate and business services (except ownership of dwellings and social and personal services).

Estimates of GDP for the following activities not covered by the surveys of establishments, mentioned above, are calculated on the following bases:

8.5.1.1.1 Agriculture and Fishing

The participation of this sector in the GDP is 4.4 percent according to the recently published GDP. This sector includes crops, livestock and livestock products, and fishing. Data collection is based on the following:

i) Crops: Data concerning crops are collected by a survey carried out by the Ministry of Agriculture and Water, which provides figures of quantities produced and wholesale prices. Gross output is estimated by multiplying figures of quantities produced by figures of market prices, less margins for trade and transport. Calculation of intermediate consumption is based on studies on cost of production carried out by the National Accounts section of the CDS.

ii) Livestock and Livestock Products: This category includes breeding of camels, cows, sheep, goats, poultry

and production of dairy products and eggs. Data concerning livestock are based on estimates supplied by the Ministry of Agriculture and Water, plus livestock imported for breeding purposes. Data for intermediate consumption are based on studies conducted by the Agriculture College of King Saud University.

iii) Fishing: Due to lack of statistics on fishing, the data mainly depend upon the those supplied by the Ministry of Agriculture and Water. Gross output is estimated by multiplying quantity data provided by the Ministry of Agriculture and Water by producers' prices, which are estimated using retail prices of fish, adjusted for selling and transport costs. Intermediate consumption is estimated using the relationship between gross output and intermediate consumption obtained from studies on production costs.

8.5.1.1.2 Extraction of Crude Oil and National Gas

The main sources of data for this sector are the annual reports of oil companies submitted to the CDS. These include details of revenues, stocks, costs and capital expenditures, for different activities. However, data included in these reports have to be adjusted for the purpose of preparing national accounts. This is because the accounting systems of these companies are based on the US and UK styles which pay little attention to the accounting information needs of national accounts (see chapter 6).

In addition, most oil and natural gas companies prepare their financial reports in accordance with the Gregorian calendar, because most of their activities involve dealings with international companies which follow that calendar, while national accounts are prepared in accordance with the Hegira calendar. Because of the difference between the two calendars, other adjustments also have to be made (interview No. 2). Nevertheless, this problem may be overcome by the recent change in the fiscal year of the State in Saudi Arabia (see chapter 7).

8.5.1.1.3 Mining Activities (Excluding Petroleum)

The activities in this sector are largely limited to the extraction of sand, stone and gravel for construction, and no satisfactory data on revenues or costs are available. However, their contribution to the total GDP is relatively small. GDP in mining is estimated by taking a percentage of the GDP figure for construction and gross output is estimated by taking a percentage of the GDP figure for mining. These percentages are based on investigations of mining activities by the CDS.

8.5.1.1.4 Manufacturing

This sector includes the following activities:

1. Food and beverages
2. Textiles and clothing
3. Leather products
4. Wood products

5. Paper products and printing
6. Chemicals, rubber and plastics
7. Ceramics and glassware
8. Construction materials
9. Metal products, machinery and equipment
10. Other manufacturing

The main sources of data concerning the above activities are the yearly survey carried out by the CDS, the value of loans provided by Saudi Industrial Development Fund (SIDF) and the number of licences issued by the Ministry of Industry.

8.5.1.1.5 Electricity, Gas and Water

The data required for calculating gross output and intermediate consumption for electricity are provided by Electricity Companies, for gas by the Gas and Manufacturing Company and for water by the Water Departments, in their annual reports submitted to the CDS which include data related to their revenues, expenditures and capital formation.

With regard to water distributed by establishments other than the Water Departments, the data are obtained from surveys of establishments carried out by the CDS.

8.5.1.1.6 Construction

Construction activity has witnessed considerable expansion in recent years due to the active role played by the Real Estate Development Fund (REDF), the Ministry

of Public Works and Housing and the Ministry of Municipal and Rural Affairs, in developing this sector.

The contribution of the construction sector to the GDP is estimated as a percentage of the total expenditure on construction made by all sectors of the economy. These sectors are as follows:

i) Government-financed construction: this is based on classification of government capital expenditure according to type of assets.

ii) Construction by government enterprises: this is calculated from annual returns supplied by them to the CDS giving details of their revenue and expenditure.

iii) Gross output in the oil sector: this is supplied by the oil companies in their annual returns to the CDS, referred to earlier.

IV) Other construction: Gross output is based on results of surveys of establishments conducted by the CDS.

8.5.1.1.7 Wholesale & Retail Trade, Restaurants & Hotels

The main sources of data for the estimation of this activity are the regular surveys carried out by the CSD, which provide figures on value of purchases, sales, salaries and wages paid, newly-purchased fixed assets, and all other expenditures and revenues. The product of the wholesale and retail trade is estimated as the difference between the value of sales and purchases from goods bought for the purpose of resale, without any change in their current condition in terms of appearance or

contents. The product of restaurants and hotels is estimated by revenues against provision of meals, residents and services. Revenues are also used as an indicator to complete the estimation of wholesale and retail trade, while the number of occupied rooms and residents and the total of revenues are used as indicators for hotels.

8.5.1.1.8 Transport and Communication

Most infrastructure projects in the transport and communications sector were completed during the Fourth Development Plan (1985-1990). These included road, railways, airports, seaports, post, telephone, telex and other telecommunications facilities. For the purpose of calculating GDP, this sector is divided into government transport and communication enterprises, and non-government transport enterprises.

i) Government Transport and Communication Enterprises

This includes the national airline and railway. Gross output and GDP for these two government enterprises are calculated from annual reports sent by them to the CDS, which include data on revenues, expenditures and capital formation. This category also includes post, telegraph and telecommunication services, for which gross output and GDP are calculated from data of their revenues and expenditures available in both the budget and the final accounts of the state.

ii) Non-government Transport

Figures of GDP on road transport are calculated from estimates of the number of vehicles in use and average income from different types of vehicles. For the purpose of obtaining gross output, the relationships between gross output and intermediate consumption are calculated from the results of the CDS survey of establishments. This category includes estimates for water transport, airport and seaport services, for which gross output and intermediate consumption are calculated from data obtained from the survey of establishments carried out by the CDS. It also includes estimates for Pipeline calculated from statements on revenues, expenditures and capital formation, sent annually by the company to the CDS.

8.5.1.1.9 Ownership of Dwellings

Benchmark figures are obtained from the results of the household expenditure survey of 1977, conducted by the CDS. To obtain estimates for other years, the benchmark figures are multiplied by an index of growth, calculated from available data on house construction.

8.5.1.2 Producers of Government Services

Producers of government services covers central government ministries and departments, municipalities and public agencies with independent budgets, excluding public enterprises (e.g Railway and Saudi Airlines) which were discussed earlier under transportation. Data on

expenditure are taken from the accounts of the government, municipalities and public agencies with independent budgets published annually.

The gross output and GDP for producers of government services are obtained from classification of government consumption expenditure according to cost, consumption and purpose. This classification shows figures for compensation of employees, intermediate consumption and final consumption.

8.5.2 Government Final Consumption

This table includes three columns, namely: compensation of employees, intermediate consumption and final consumption expenditure. The total of each column is classified according to purpose, using the categories recommended by the UN system of national accounts.

This account is prepared by classifying and aggregating current expenditures of (a) central government ministries and departments (b) municipalities and (c) departments with independent budgets, from their expenditure accounts, available annually.

As far as the sources of data are concerned, data related to central government ministries and departments are supplied by the Ministry of Finance and National Economy; data related to municipalities are obtained from the annual statements of actual revenue and expenditure of each municipality; and data related to departments with independent budgets are taken from their annual reports.

8.5.3 Gross Fixed Capital Formation

Gross capital formation is classified into the following categories:

1. Residential Building Construction;
2. Non-Residential Building Construction;
3. Other Construction;
4. Transport Equipment; and
5. Machinery and Equipment.

Each of the above categories is further classified under government sector, non-oil private sector and oil sector. As far as the sources of data are concerned, these vary according to the sector concerned.

Data for the government sector are obtained from a classification of its capital expenditure by type of asset using central government accounts, municipalities and departments with independent budgets.

In the case of the non-oil private sector, capital formation in dwellings is available from the calculation discussed earlier (see sec. 8.5.1.1.8). Figures for government enterprises included in the non-oil private sector are shown in their annual returns to the CDS. Capital formation in agriculture is estimated using figures for loans given by the Agricultural Bank for purchase of machinery and other equipment. For other capital formation in the non-oil private sector, the main sources of data are the Surveys of Establishments carried out by the CDS.

Capital formation in transport equipment by transport operators without a fixed location, is

estimated separately, because they are outside the scope of the surveys of establishments. It is calculated from estimates of the number of new vehicle registrations.

Finally, with regard to the oil sector, the main source of data for capital formation is the annual returns of oil companies submitted to the CDS (see sec. 8.5.1.1.2).

8.5.4 External Transactions

This account represents the current and capital transactions of the nation with the rest of the world. However, due to lack of data on capital transactions, this account only shows figures of current transactions.

The main source of data is the annual balance of payments statement which is prepared by the Saudi Arabian Monetary Agency (SAMA). Data on merchandise exports and imports are supplied by the foreign trade section of the CDS, while data on exports and imports of services are estimated from data provided by SAMA.

8.6 Users of National Accounts in Saudi Arabia

National accounts are mainly prepared for use by those organisations responsible for planning at the national level, including the Ministry of Planning, Ministry of Finance and National Economy, and the Saudi Arabian Monetary Agency. They also used by International Financial Institutions such as the International Monetary Fund (IMF) (interview No. 12)

8.7 Problems of Constructing National Accounts in Saudi Arabia

Based on interviews conducted with national accounts section officials, and a review of recent published national accounts, the following are the main problems relating to the national accounts in Saudi Arabia:

1. lack of statistical data;
2. shortage of qualified manpower; and
3. absence of a linkage between the micro and the macro accounting systems.

These problems are discussed in further detail below.

8.7.1 Lack of Statistical Data

The lack of availability and the unreliability of the statistical data necessary to construct national accounts are not unique to Saudi Arabia. This is very clear from the observation of Enthoven (1977, p.62):

"In most developing economies, it has been difficult to construct a set of Macro [national] accounts. Statistical and accounting data are either lacking or deficient. For example, a large portion of agricultural production may not go through the market system, making it difficult to estimate; many people may perform various jobs and incomes may be paid in commodities."

Indeed, all three top national accounts officials interviewed explained that the input data needed to construct national accounts are not available either on time or in the proper format. One of the three stressed that the government accounts are kept on a strictly cash basis, which makes it difficult to measure the state's

capital formation. This is because the cash basis does not recognize capital assets obtained by means other than cash (e.g. loans or grants), since no cash is involved in such transactions (see chapter 7). Furthermore, he mentioned that since 1985 it has become difficult for the national accounts section to obtain the state's final accounts.

In addition, most data required for the construction of national accounts, except those from government and oil companies, are collected through surveys of establishments. These surveys are carried out by the CDS in the form of questionnaires sent to the establishment concerned. However, an examination of the blank form of one of these questionnaires (see figure 8.3) and consideration of the method of distribution, suggest that this approach suffers from the following deficiencies:

First, the survey does not cover all economic units, and omits many medium and small units;

Second, the questionnaire does not include details related to value added, which is a major element of national accounts;

Third, the date printed on the form suggests that it was designed many years ago and has been used without any change in its classifications; the only amendment is to delete the old date by crossing it in ink, and to write in the current year's date;

Figure 8.3
A Form of Data Collection for Livestock Products

General Data

Farm Name: Date of Establishment:
 Address of the Farm: Economic Activity:
 Date of commencement of actual activities:
 Period of Research From: To:

1. Employees in the Farm

Saudi	Non-Saudi	Total

A) Administrators

b) Supervisors

C) Other Employees

2. Salaries and Wages Throughout the Year

	Saudi	Non-Saudi	Total
- Salaries and Wages in cash			
- Incentives (non-Monetary)			
- Others			

3. Cost of Production

Value in Saudi Riyals

1) _____

2) _____

3) _____

4. Value of Production

1) Sales Value

2) Opening Stocks

3) Closing Stocks

5. Government Subsidies

--

Source: Central Department of Statistics (CDS), National Accounts Section (Author's Translation).

Fourth, the statistical data gathered by this approach lack comparability because of the diversity of accounting procedures and policies applied by the economic units in question; and

Finally, the survey of establishments is hampered by a lack of cooperation between the respondents and the data collectors.

Evidence of the problems associated with the statistical data can be easily found. For example, when looking at any recent published national accounts one finds that the phrase "due to lack of data ..." appears frequently under various headings.⁷

Due to the inadequacy of data, no single method of estimation is used. Instead, estimates are based on a combination of sources and methods, with national accountants sometimes using guesswork to complete their estimates. It is, therefore, very difficult to rely on the information produced.

8.7.2 Shortage of Qualified Manpower

As far as the shortage of qualified manpower is concerned, the total number of staff involved in the preparation of national accounts is fifteen persons (interview No. 10). However, only three of these are actually involved directly in the preparation of national accounts. This small number is unable to cope adequately with the generation, selection and evaluation of data for

⁷ For example, See National Accounts of Saudi Arabia, CDS, December 5, 1983, pp. 18, 19, 21; 1987, p.23.

national accounts purposes. It is extremely difficult to find qualified statisticians, and the current training facilities in the field of national accounts are inadequate. No special statistical institute exists in Saudi Arabia, and the current accounting and economics programmes offered by Saudi universities pay little attention to the measurement and processing of data for national accounts purposes (see chapter 4). Currently, training of national accounts staff mainly takes place in the United States, for a period ranging from six months to one year. This period of training is considered by the national accounts staff to be inadequate, taking into account the English foundation courses which are included in the programme period.

Furthermore, one of the officials indicated that in order to overcome the problem of shortage of staff the national accounts section sometimes hires part-time staff, mainly school-teachers, (interview No. 2).

8.7.3 Absence of Linkage between the Micro and the Macro Accounting Systems

A number of accounting authors have expressed their concern about the importance of micro accounting information for the purpose of constructing macro accounts. Briston (1981a, p. 490), for example, states:

"... the quality of the social [macro] accounts depends to a large extent on the quality of the accounting system of individual economic entities as the macro estimates are derived from the data generated at the micro level."

In demonstrating how micro accounting information would be useful for macro accounting purposes, Lubbert (1965, p.57) stated that the National Income and Product Account "can be derived conceptually by a consolidation of the profit and loss statements of all economic units that participate in creating the national product."

In Saudi Arabia, there is no linkage whatsoever between the micro and the macro accounting systems. The enterprise accounting system, as discussed earlier (see chapter 6), is designed to provide information for external users (mainly shareholders), while the government accounting system (see chapter 7) is designed to provide information related to public accountability. Even the recent accounting approach developed in Saudi Arabia omits the accounting information needed by macro accounting (see chapter 9).

Accordingly, integration between the individual accounts of micro units is urgently needed in order to provide better information for the purpose of constructing macro accounts. The only way this task can be achieved is by the adoption of a uniform accounting system by all micro units.

8.8 Proposals For Improvement

Having considered the major problems encountered by national accounts in Saudi Arabia, it is possible now to suggest some means by which these problems might be alleviated. These include the following proposals:

1. Cooperation between accountants in industry, the accounting profession, and CDS staff must be established to collect the necessary data required by national accounts.

2. The surveys of establishment should be extended to cover all economic units, including medium and small units.

3. The forms designed by the CDS for collecting data for national accounts should be amended to generate more relevant data. Moreover, these forms should be accompanied by guidelines explaining how they should be completed and assuring the respondents that such data will remain confidential.

4. Government units should cooperate with the CDS by sending their final accounts and other related reports on a regular and timely basis.

5. Linkages between the micro and the macro accounting systems should be established. Thus the accounting systems (formats, classifications, policies and procedures) of individual economic units should be designed to produce accounting information relevant to the construction of national accounts. The greater the conformity between enterprise and government accounts and

the classifications used for the national accounts, the easier it will be to construct the national accounts, and the better their quality.

6. National accounting should be included in the accounting programmes currently offered by Saudi Universities so that accounting graduates are equipped with basic knowledge of this vital subject.

7. The training period of national accounts staff may have to be extended to two years or more to enable trainees to acquire sufficient knowledge and experience in the field of national accounts.

8. A computer network should be established between the CDS headquarters and its branches throughout the Kingdom on the one hand, and other economic units on the other, to generate better and more timely accounting data.

8.9 Summary and Conclusion

The purpose of this chapter has been to examine the national accounts system in Saudi Arabia in order to ascertain whether it provides reliable accounting information for the purpose of planning and control at the national level.

The chapter reveals that the national accounts in Saudi Arabia are based on the UN system of 1968. However, due to the lack of statistical data and other problems, the UN system is not comprehensively implemented. As a result, the national accounts currently prepared by the CDS do not include input-output tables, a flow of fund

statement, and a national balance sheet. The main reasons for the absence of these tables, according to national accounts officials, is the absence of data on which to base them.

There are no statutes or professional accounting regulations that require companies to prepare and publish financial information for the purpose of national accounts. Indeed, even the recently stated objectives of financial statements in Saudi Arabia exclude the accounting information needed by government for the purpose of national accounts, merely saying that the government has the ability to obtain the information that it needs. However, nothing is mentioned about how and when such information can be obtained. Much, therefore, needs to be done to improve national accounts in Saudi Arabia. Perhaps the most urgent need is to have a more uniform system of accounts and better definitions of accounting data. Such improvements must be seen in the context of overall accountancy development and should be reflected in all components of the accounting system (education, profession, enterprise government and national accounting).

PART III

RECENT POSITION AND FUTURE

CHAPTER 9

RECENT ACCOUNTING GUIDELINES IN SAUDI ARABIA: REVIEW AND EVALUATION

9.1 Introduction

The main interest in accounting at the present time at the domestic level appears to be the formulation of accounting standards (Samuels and Piper, 1985). Saudi Arabia seems to be no exception; in recent years the Ministry of Commerce, which monitors the accounting and auditing profession, agreed to finance a project to develop accounting and auditing standards. The project was carried out by a team of accounting experts from the UK and the US as well as Saudi Arabia.

It appears from the Analytical Study attached to the statements published so far that the working team has considered two types of accounting systems. The first is a flexible accounting system which allows a wide choice among different accounting methods and procedures for the same transaction, as is found in the UK and the US. The second is a uniform accounting system, in which accounting methods and procedures are established on a uniform basis, as is found in the France and Tunisia.

Although both systems were considered in the comparative stage of the programme, preliminary findings published so far suggest that the first approach, i.e. a flexible accounting system, biased toward the American and British style, has been chosen as the path for developing accounting in Saudi Arabia.

The purpose of this chapter is not only to describe recent accounting developments in Saudi Arabia, but also to evaluate the approach adopted and the contents of the accounting guidelines established so far.

This chapter, therefore, is divided into a number of sections. The next section considers the objectives and users of financial reports in the UK and the US. In section three, Saudi Arabia's experience in developing its own accounting and auditing standards is examined. Section four provides an overview of the accounting guidelines established so far. In section five, these guidelines, together with the adopted approach, are critically evaluated in the light of the prevailing conditions and circumstances of accounting environment in Saudi Arabia. Finally, a summary and conclusion drawn from the discussion throughout this chapter will be presented in section six.

9.2 The Objectives and Users of Financial Reports in the UK and the US

No comprehensive set of objectives of financial reports has been developed in the UK. However, the Boothman Committee (the British counterpart of the Trueblood Committee in the US) was formed by ASSC in 1974 and had as its terms of reference the re-examination of the scope and aims of published financial reports in the light of modern needs and conditions. The results of the study were published in the Corporate Report in 1975. This report argued that:

"the fundamental objective of corporate reports is to communicate economic measurements of and information about the resources and performance of the reporting entity useful to those having reasonable rights to such information." (the Corporate Report, 1975, P.28).

With regard to the users of financial statements, the Corporate Report identified the following groups as those who have a reasonable right to information and whose information needs should be considered:

- (a) The equity investor group including existing and potential shareholders and holders of convertible securities, options or warrants.
- (b) The loan creditors group including existing and potential holders of debentures and loan stock, and providers of short term secured and unsecured loans and finance.
- (c) The employee group including existing, potential and past employees.
- (d) The analyst-adviser group including financial analysts and journalists, economists, statisticians, researchers, trade unions, stockbrokers and other providers of advisory services, such as credit-rating agencies.
- (e) The business contact group including customers, business rivals, and those interested in mergers, amalgamations and takeovers.
- (f) The government including tax authorities, departments and agencies concerned with the supervision of commerce and industry, and local authorities.
- (g) The public including taxpayers, ratepayers, consumers and other community and special interest groups, such as political parties, consumer and environmental protection societies and regional pressure groups. (Ibid. P.17).

In addition, the Boothman Committee stated that to meet the varied information needs of these users, new forms of accounting disclosure were required.

Accordingly, the committee recommended the following six additional statements:

1. A statement of value added.
2. An employment report.
3. A statement of money exchange with government.
4. A statement of transactions in foreign currency.
5. A statement of future prospects.
6. A statement of corporate objectives. (Ibid. P.79)

Nevertheless, these "recommendations have yet to be taken up by the profession and corporate reports in the business sector have largely remained concerned with fulfilling the statutory duties relating to reporting profits and loss" (Jones and Pendlebury, 1984).

In the United States, the FASB Statement of Financial Accounting Concepts No. 1, entitled "Objectives of Financial Reporting by Business Enterprises," was issued in 1978. It laid down the following objectives:

1. To provide information which is useful to investors, creditors, and others in making rational decisions.
2. To assist investors and creditors in assessing future net cash flows to the enterprise in respect of amount, timing, and uncertainty.
3. To identify entity resources (assets) and claims against resources, both creditor claims (liabilities) and owner claims (owners' equity).
4. To provide information about enterprise performance and earnings potential.
5. To show how an enterprise obtains resources and how it uses them.

According to FASB statement No.1, users of financial statements are primarily investors and creditors, whose information needs are defined by the statement as being:

"information for predicting, comparing and evaluating enterprise earning power and to judge the management's ability to utilize enterprise resources in achieving earnings and cash flow."

From the foregoing brief discussion it appears that the main objective of financial statements in the UK and in the US is to provide information in respect of listed companies for stockholders and potential investors. Although the Corporate Report in the UK mentioned the government among the user groups, it specified no needs other than tax purposes and the need to monitor compliance with government laws and regulations.

However, accounting standards should evolve from the environment that they serve. Since environmental characteristics differ from one country to another, it is unlikely that the standards which evolved in one country under particular circumstances will satisfy the needs of another country. This idea has been discussed by a number of accounting authors. Briston (1978), for example, criticises the adoption of accounting principles and system of the UK and the US by some developing countries on the ground that such a system no longer even meets the needs of its own environment. Instead, Briston encourages developing countries to create their own accounting system.

"... instead of recognising the inadequacies of the UK/US system and attempting to make it more relevant and integrated, UK/US accountants are gradually imposing that outmoded system upon developing countries. On the contrary,

developing countries must create their own systems before this adverse influence has reached an irreversible stage. ... Each country should be encouraged not to standardise the structure and specifications of its information system, but to create a system appropriate to its own needs." (Briston 1978, pp.119-20).

Thus it may be concluded that the accounting system of the UK and the US may not even meet all the needs of its own environment, and is certainly not relevant to the environment of Saudi Arabia, which has no official stock market, a lack of accounting skills, and where the number of listed corporations is far lower than in the UK and the US.

9.3 The Development of Accounting and Auditing Standards: Saudi Arabia's Experience¹

9.3.1 The Development Programme

The development programme was a private sector initiative financed by the Ministry of Commerce and initiated by Abdul Aziz Al-Rashed, managing partner of a leading Saudi accounting firm, Al-Rashed Certified Public Accountants. The development programme consisted of several stages and lasted for about six years.

9.3.1.1 The Preliminary Study

The preliminary study was completed in 1400H (1980), and acknowledged that economic activities in Saudi Arabia were undergoing enormous changes in every respect. The requirements of users of the profession's services had

¹ Part of this section is based on Al-Rashed, A. "The Development of Accounting and Auditing Profession in Saudi Arabia", Paper presented at Seminar on Accounting and Auditing Standards, Bahrain, February 1987. A personal interview was also conducted by the author with Mr. Al-Rashed himself in December 1989.

changed greatly, and the profession had not developed means to meet these challenges. The study concluded with a statement highlighted the major deficiencies of the accounting profession which include non-availability of generally accepted national accounting standards, generally accepted national auditing standards, a comprehensive ethical code, and a specialized body to sponsor the profession (Al-Rashed, 1987).

The results of the preliminary study were discussed in the first accounting conference of its kind held in Saudi Arabia in 1981 at King Saud University, and, together with the recommendations which came out of this conference, were submitted to the Ministry of Commerce. The Ministry further studied and discussed the proposals and finally agreed to finance the project (interview No. 11).

9.3.1.2 The First Stage of the Development Programme: the Comparative Study

A comparative study of the accounting systems of other countries is important in order to establish an accounting system relevant to the local environment's needs. Briston (1978, p.117), for example, states:

"A comparative study of the evolution of accounting under different environments should provide important lessons regarding the true nature of accounting and the extent to which it is possible to separate the fundamental truths from the historical accidents."

Nobes and Parker (1985) also supported this idea and argued that "Comparative accounting is important because

it allows us to study solutions to problems which have been proposed but not adopted in home countries. It also makes it easier to predict how successful attempts at harmonisation are likely to be."

Indeed, the importance of the comparison of various accounting systems was recognized by the team appointed to develop accounting and auditing standards in Saudi Arabia. For this purpose, nine countries were identified and classified into three groups based on (1) the state of development of their accounting profession; (2) the similarities of their economic circumstances to those of Saudi Arabia; and (3) the ability of Saudi Arabia to benefit from their established organisations. These groups were as follows (Statement of Accounting Objectives and Concepts, 1986, p.136):

- The first group included United Kingdom, United States, and Canada;
- The second group included France, West Germany and Sweden;
- The third group included Tunisia, Venezuela, and Brazil.

From the above groups, United States, West Germany and Tunisia were selected for the comparative study. This stage of the development programme involved the following actions:

- A. Review of laws, regulations, professional bulletins, and any other related material:
1. Accounting Standards and Financial Reporting Requirements
 2. Auditing Standards and other Auditing Requirements

3. Professional Code of Conduct
 4. Profession Internal Organisation
- B. Interviews with those responsible for the profession in the three countries.
- C. Analysis of data gathered in the previous stages
- D. The end report was prepared and translated into Arabic by experienced professionals in the same field. It discussed all features of the profession in every country and a detailed plan for the second stage (Ibid.)

9.3.1.3 The Second Stage of the Programme: Areas Selected for Development

Based on the results of the first stage, two options were considered for development in the second stage, namely (1) starting a comprehensive plan to deal with all deficiencies at the same time or (2) concentrating on solving the more urgent deficiencies in the profession only. Taking the time factor and the urgent need for development into account, the second option was adopted and the following aspects of the profession were selected for development:

A. Selected subjects from financial accounting:

- 1) Determination of the objectives of financial accounting;
- 2) Definition of the most important concepts of financial accounting;
- 3) Preparation of standards of general presentation and disclosure.

B. Auditing Standards.

C. Internal organisation of the profession

Each of the above areas was assigned to a particular team. Care was taken to involve, in each team, highly experienced technical experts from the selected countries who were familiar with the Arabic language. Saudi professors and advisers were selected to give their assistance. The group in charge of the project was also represented. Several meetings were arranged to discuss and exchange ideas among the teams (Al-Rashed, 1987).

9.3.1.4 The execution of the Second Stage

Several steps were involved in implementing the second stage. These can be summarized as follows:

- a) A background study was prepared about the current status of the profession in the Kingdom and regulations that affect the profession and was distributed to members together with copies of those regulations in both Arabic and English.
- b) A number of visits were arranged for the members of the teams, who reviewed actual audit cases and became acquainted with circumstances in the Kingdom.
- c) Visits were made to the related institutions and discussions were conducted to determine the best means of cooperating with and encouraging contributions from those institutions.
- d) The basis of the preparation of the features selected for development of the profession and the selection methodology of the scheme, its preparation and presentation were agreed.
- e) A preliminary draft was prepared by each team. It was reviewed by the adviser and those in charge and then returned to the members of the teams.
- f) A second draft was prepared and distributed among the teams for familiarisation, review, and comment by the advisers and those in charge.

- g) The comments were gathered and a meeting was held in Riyadh and attended by all team members, to exchange findings and ideas.
- h) The recommendations were reviewed in a meeting attended by the officials of the Ministry of Commerce and other related Ministries.
- i) The comments raised during the two meetings mentioned in (g-h) above were noted.
- k) One of those working on the project was appointed to read all the reports prepared by all teams before it finalised.
- l) The final report was reviewed by a high committee of Chartered Accountants in the Ministry of Commerce, and distributed to selected licensed auditors for review and comments.
- m) The comments received from the above-mentioned were tabulated, reviewed, and commented on by the Ministry of Commerce.
- n) The final report was approved and issued by the Ministry of Commerce to be used by all concerned as formal guidelines (Ibid.).

9.3.2 Approaches Considered For the Development of Accounting and Auditing Standards in Saudi Arabia

Four alternative approaches were considered by the working team in order to select the one most suitable for Saudi Arabia. These approaches were as follows:

- 1) The adoption of standards from other countries;
- 2) The adoption of the International Accounting Standards and International Audit Guidelines;
- 3) Application of the induction technique;
- 4) Application of the deduction technique.

To ensure the applicability of the approach adopted, it was decided to establish criteria against which these approaches might be evaluated. Taking the urgency of the matter into consideration, the approach to be adopted had to:

- 1) provide a reasonable degree of assurance that the standards would be relevant;
- 2) provide a reasonable degree of assurance that the standards would be acceptable;
- 3) provide a reasonable degree of assurance that the standards established would be consistent; and
- 4) take into account the status of the profession of accounting and auditing in Saudi Arabia (Ibid).

After detailed study and evaluation of the approaches against the established criteria; and taking into consideration the urgency and the present status of the accounting profession, none was found to be acceptable. Accordingly, an alternative approach had to be found, and this is considered next.

9.3.3 Saudi Arabia's Approach

The approach adopted consisted of three phases (see figure 9.1):

Phase 1 Defining the overall objectives of financial accounting or auditing in Saudi Arabia

This phase involved examination of the economic, social, political, legal and business environment in Saudi Arabia; and consideration the current and potential role of accounting and auditing, and the state of professional practice in Saudi Arabia. Based on this, a statement of accounting and auditing objectives in Saudi Arabia was drafted.

Phase 2 Identification of the basic concepts of accounting and auditing in Saudi Arabia.

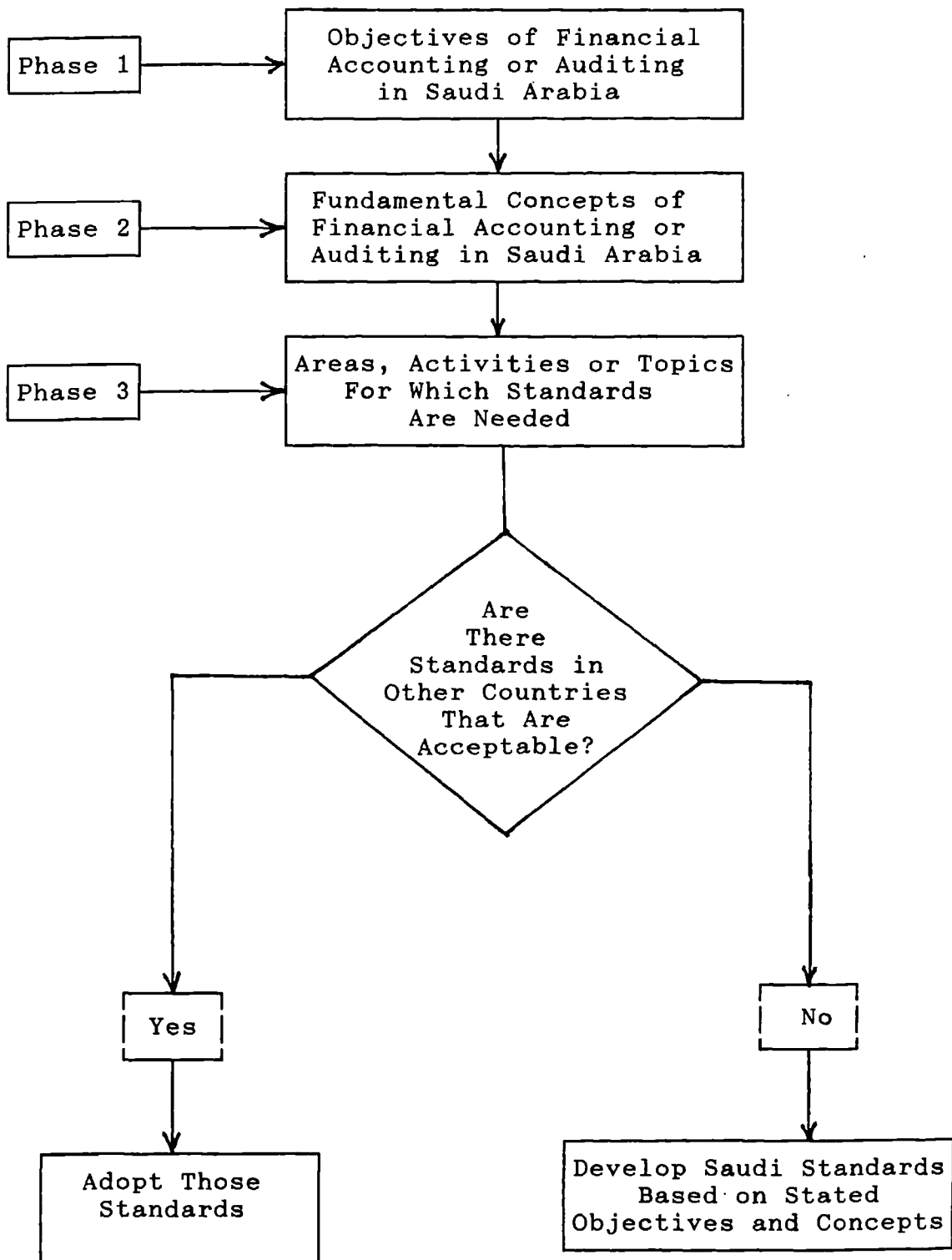
This phase was based upon the previous phase and resulted in a set of basic accounting and auditing concepts.

Phase 3 Establishing Detailed Standards for Financial Accounting and Auditing in Saudi Arabia

This was the final phase and involved several tasks:

- 1) Identifying the activities, topics or areas of financial accounting and auditing for which standards are needed;
- 2) Defining the issues under each activity, topic or area for which standards are needed;
- 3) Reviewing standards developed in other countries to deal with the issues defined in (2) above;
- 4) Evaluating standards developed in other countries to determine their acceptability in relation to the objectives, limitations and fundamental concepts of financial accounting and auditing in Saudi Arabia;
- 5) If a standard developed in another country was found to be acceptable based on the evaluation in (4) above it would be adopted;
- 6) If no standard developed in another country was found to be acceptable based on the evaluation in (4) above, a Saudi standard consistent with the objectives, limitations and fundamental concepts would be developed. (Al-Rashed, 1987).

Figure 9.1
Saudi Approach for Establishing Accounting
and Auditing Standards



9.4 Review of the Accounting and Auditing Guidelines Established so far in Saudi Arabia

The first output of the accounting development programme was published in two volumes. The first volume, entitled "Accounting Objectives and Concepts", includes three topics as follows:

- 1) Financial Accounting Objectives;
- 2) Financial Accounting Concepts;
- 3) Standard of General Presentation and Disclosure.

The second volume, entitled "Auditing Standards", includes seven standards as follows:

- 1) Standard of adequate professional competence;
- 2) Standard of auditor's neutrality and independence;
- 3) Standard of due professional care;
- 4) Standard of auditing planning;
- 5) Standard of documentation and control;
- 6) Standard of auditing evidence;
- 7) Standard of auditing reports.

The contents of both volumes were approved and issued by the Minister of Commerce's Decision No.692 dated 28/2/1406 H. (1986) "to be used by all concerned as formal guidelines".

9.4.1 The Statement of Financial Accounting Objectives

The Statement of Financial Accounting Objectives concentrates on the needs of external users of financial reports. It was stated in its introduction that the principal objective of this statement (para 51) is:

- 1) To assist agencies concerned with establishing financial accounting standards by guiding their efforts so that this statement can serve as a basis for devising those standards.
- 2) To assist certified accountants and others (such as an entity's management) in determining the proper accounting treatment of matters for which no financial accounting standards have yet been issued.
- 3) To increase users' understanding of information contained in the financial statements and the limitations of applying this information.

The statement discusses various areas of financial accounting including determination of users of financial statements, their common needs, objectives of general-purpose external financial statements and their limitations. For example, the statement determines the users of financial statements (para 53) as:

"the present and potential investors, creditors, suppliers, and customers. ... Although other external agencies (such as the Department of Zakat and Income Tax and government agencies directing legislation and planning the national economy) benefit from these statements, these agencies were not focused on when determining the objectives of general purpose financial statements. This is because they have the ability by virtue of their authority, to determine the information that should be presented to them by an enterprise to meet their needs."

The Analytical Study attached to the statement provides more detail concerning the characteristics of the above users (see figure 9.2). For example, at the outset the users of financial statements are divided into two main groups, as follows (para 105):

A. Users with a direct interest in an enterprise

This group includes present investors (owners equity) and future investors and lenders (present and potential), the Department of Zakat and Income Tax, grant-providing government agencies, and an enterprise's management, employees, customers, and suppliers.

B. Users with an indirect interest in an enterprise

This group includes government control departments, and government agencies responsible for planning and directing the national economy.

Users in the above two main groups are further divided according to their ability or authority to determine the information that they require from an enterprise into two groups as follows:

A. Users having the ability or authority to determine the information that they require from an enterprise

This group includes the Department of Zakat and Income Tax, grant-providing government agencies, an enterprise's management, government control departments, and government agencies responsible for planning and directing the national economy.

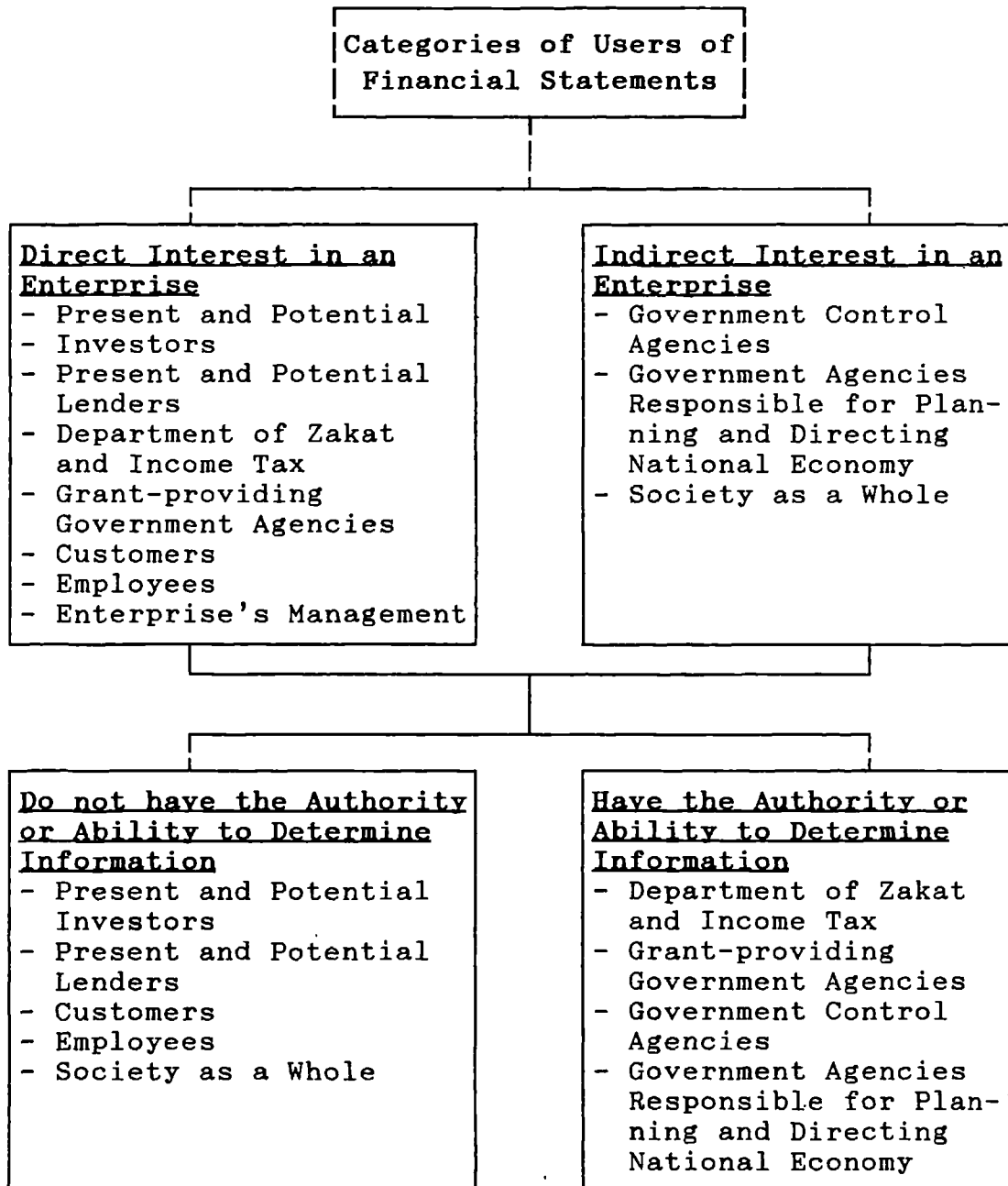
B. Users not having the ability or authority to determine the information that they require from an enterprise

This group includes the remaining users although some lenders may have the ability to determine some of the information that they require from an enterprise.

Financial decision-making is considered as the principal use which is shared by all major users. Such

decisions mainly depend upon the ability of the enterprise to generate cash flow. (para 54).

Figure 9.2
Users of Financial Statements in Saudi Arabia



Source: Objectives and Concepts of Accounting in Saudi Arabia - Analytical Study, 1986, p. 165

After identifying user groups and their needs, the statement deals with the objectives of financial statements as follows (para 70-76):

- 1) Providing appropriate information to satisfy the needs of major users.
- 2) Periodic measurement of an enterprise's income.
- 3) Providing information to assist in evaluating an enterprise's ability to generate cash flows.
- 4) Providing information about an enterprise's economic resources and their sources.
- 5) Providing information about the sources and application of funds.

In order to determine the objectives of financial statements in Saudi Arabia, comparison was made with their equivalent in the US, West Germany and Tunisia. However, a close look to the above objectives reveals that they are similar to those of the United States (FASB's statement No.1). The similarities are represented by the emphasis placed on the common needs of external users, particularly those of investors and lenders, for information required to assist them in evaluating the expected probabilities of cash flows, and that a great portion of this information should be presented to them through the financial statements.

In addition, the statement finishes with some limitations on the objectives stated above. For example, it is stated that some information may not be contained in external financial statements, or may be contained in such a form that it can not be applied directly without modification. Examples include information needed for

determination of an enterprise's zakat, government grants, estimation of the social cost of an enterprise's operations, preparation of national accounts, measurement of value added by an enterprise to the national economy, and performance evaluation of an enterprise (para 77-82).

9.4.2 The Statement of Financial Accounting Concepts

It was stated that the objective of the Statement of Financial Accounting Concepts is to define the basic elements of financial statements of profit-directed enterprises, concepts which should govern the measurement of these elements, and characteristics of information that should be disclosed by the financial statements. (para 233)

At the outset the statement defines the phrase concept as "a basic term given a certain meaning. A term is considered basic whenever it is necessary to refer to it frequently, either explicitly or implicitly, when developing accounting standards, interpretations, or application". The word assets is given as an example, because many of the financial accounting standards are related to an enterprise's assets. Accordingly, the statement emphasises that reference should be made to the concept of assets when developing, interpreting and applying these standards (Objectives and Concepts of Accounting in Saudi Arabia, 1986, P.29). The statement classifies these concepts into four major types as follows:

1) Concepts of Basic Elements of Financial Statements

These types of concepts define the basic elements of financial statements, namely:

- assets, liabilities and owners' equity;
- revenues, expenses, earnings, losses, net income (or net loss), owners' equity investments, and distributions of earnings. These ten elements are combined in two groups:

- (1) The financial position elements, which include the first three elements;
- (2) The elements which represent changes in financial position and include the other seven elements (para 237).

The statement then defines each of the above elements and the basic characteristics which distinguish each element from the others (para 239-257). For example, the statement defines an asset as "anything that has the ability to provide an enterprise with services or benefits in the future and was acquired by the enterprise as a result of events that occurred or operations that were performed in the past, provided that it is financially measurable at present to an acceptable degree of accuracy, and should not be directly related to an immeasurable obligation" (para 239).

2) Concepts of Events, Transactions, and Circumstances

Events have been defined as occurrences having their effect on the accounting unit and divided into two categories: Internal events which occur within the accounting unit, and external which involve transactions between accounting units or interactions between the

accounting unit and the surrounding environment. As for the accounting measurement of these events, transactions, and circumstances, the statement provides three stages to be carried as follows (para 259):

First Stage: Accounting recognition of the events, transactions and circumstances affecting assets and liabilities.

Second stage: Determination of the value of changes in these assets and liabilities

Third Stage: Expressing these values in monetary units.

3) Concepts of Accounting Measurement

Accounting measurement involves determination of the values of all basic elements included in the financial statements of an enterprise. The basis and characteristics of accounting measurement include the following concepts: accounting entity, going concern, unit of measurement, and periodic reporting (para 266).

The above concepts are fully covered in the accounting literature. They appear to be clear and there is nothing to be gained from discussing them here again. Nevertheless, it is useful to throw some light on the unit of measurement concept, since it is considered the most important one.

The statement points out that "the monetary unit is the general unit that reflects accounting measurement (Saudi Riyal in Saudi Arabia). In the absence of considerable changes in its purchasing power, the Saudi

Riyal is considered to be a constant accounting unit of measurement" (para 275).

Although the statement emphasises the changes in the purchasing power of currency and requires this to be taken into account when preparing the financial statements, it does not recommend the application of any particular method, such as replacement cost or general price level. Nor does it mention whether such changes will be made within the financial statements or as supplementary information. In the United States, for example, statement No.33 of the Financial Accounting Standards Board, issued in 1979, recommended that firms experimented with both current cost and constant dollar accounting as supplementary information to the annual report.

4) Concepts of Qualitative Accounting Information

These concepts determine the characteristics of useful accounting information or the basic rules to be applied in evaluating the quality of accounting information. According to the statement, determination of such characteristics assists accounting standard-setting bodies and preparers of financial statements in evaluating accounting information resulting from the application of similar methods and in distinguishing between what is considered to be a necessary disclosure and what is not (para 310). Useful information is said to possess the following characteristics:

- a. Relevance.
- b. Faithfulness and reliability.
- c. Neutrality.
- d. Compatibility.
- e. Timeliness.
- f. Understandability.
- g. Materiality and optimum disclosure. (para 312)

The concepts of qualitative information suggested above are based on the recommendations prepared by the Accounting Standards Committee in England and Wales in 1975; and FASB statement No.2, "Qualitative Characteristics of Accounting Information", published in May, 1980.

9.4.2 Standard of General Presentation and Disclosure (SGPD)

9.4.2.1 Scope of the Standard

The Standard of General Presentation and Disclosure (SGPD) is the first and the only accounting standard produced in Saudi Arabia so far. As the title suggests, it deals with two topics, namely: General Presentation and General Disclosure in the financial statements. According to the preparers of the standard these are the most important areas at this stage, as accounting guidelines are needed for both statutory accountants and users of financial statements in Saudi Arabia. As for the scope of the SGPD, it was stated (para 581) that:

"This standard applies to financial statements of profit-making enterprises, regardless of their legal status or the nature of their

activities. Furthermore, this standard contains specific considerations regarding the materiality that should be taken into account in deciding whether individual accounts should be disclosed separately or can be combined with other accounts for financial statement presentation purpose. These considerations are not applicable to the other subjects addressed by the standard of general presentation and disclosure."

The SGPD set out the requirements of general presentation and disclosure in the financial statements of a profit-oriented enterprise, consolidated financial statements and financial statements of an enterprise under formation. It also lays down the treatment of accounting changes and contingent gains or losses, and requires disclosure of the definition of an entity, the nature of its activities, the nature of each of the financial statements, accounting policies, commitments, and events subsequent to the preparation of financial statements (para 578).

9.4.3.2 General Presentation

Under this heading the SGPD defines the financial statements that are to be prepared, as follows:

- 1) Statement of financial position
- 2) Statement of income
- 3) Statement of retained earnings (or statement of changes in owners' equity)
- 4) Statement of sources and application of funds

According to the SGPD, these statements and related disclosure represent the minimum requirements for the presentation of financial position, the results of operations, and the sources and application of funds

(para 583). The SGPD also ranks these statements into the above order and adds a fifth item, "Notes to the Financial Statements" (para 584).

The SGPD then mentions the criteria which should be applied when preparing each of the above financial statements. For example, the form, terminology, and elements should be classified in such a manner as to ensure easy understanding of significant information contained in these statements. All non-significant accounts should be grouped with other similar accounts. Disclosure of all values in the financial statements should be to the nearest Saudi Riyal or to the nearest thousand Saudi Riyals, depending on the magnitude of the balance (para 589). Each financial statement should be given a title to express its contents, and should state the entity's name and its legal form (e.g. joint stock company, limited liability company, joint venture etc.) and the accounting period(s) covered by the financial statements (para 591).

In addition, the SGPD states the items that should be presented in each of the above financial statements. For example, the financial position should include all assets, liabilities and elements of owner's equity including a current description of all these items or groups (para 592). Moreover, the assets shall be shown in the statement of financial position according to the following sequence:

- a. current assets
- b. investments and financial assets
- c. fixed assets
- d. intangible assets (para 593).

Liabilities shall be shown in the statement of financial position according to the following sequence:

- a. current liabilities
- b. non-current liabilities (para 594).

The SGPD also discusses the subject of materiality under the general presentation requirements. For example, it states (para 585) that:

"An individual account or group of accounts is considered to be material if its omission, non-disclosure, or improper presentation causes deviation or distortion to the information presented in financial statements or this information is inadequate to evaluate the performance of an entity".

Meanwhile the SGPD suggests guidelines which should be taken into account when determining the materiality of the value of a certain account or group of accounts. The suggested guidelines are as follows (para 587):

1. The value is considered to be material (of relative significance) if it is equal to or more than 10% of the relevant base value, unless there is evidence to the contrary.
2. The value is not considered to be material if it is equal to or less than 5% of the relevant base value, unless there is evidence to the contrary.
3. If the value lies between 5% and 10% of the relevant base value, materiality becomes subject to professional judgement depending on prevailing circumstances.

The SGPD also provides an illustrative forms for each of the four financial statements mentioned above; these are not mandatory but are intended as guides to

assist the preparers of financial statements. These forms are reproduced in Appendix D.

9.4.3.3 General Disclosure

Under this heading, the SGPD sets out the requirements of disclosure in financial statements regarding the following:

- a. Nature of an enterprise's operation.
- b. Significant accounting policies.
- c. Accounting changes, including their accounting treatment.
- d. Potential gains and losses, including their accounting treatment.
- e. Financial Commitments.
- f. Subsequent events (para 679).

The SGPD then discusses these items in detail (para 680-713) and nothing is to be gained by repeating that discussion here. However, it should be pointed out that the SGPD refers to "significant accounting policies" but does not determine what is meant by such policies. In the UK, for example, the SSAP2 issued in November 1971 defines Accounting Policies as "the specific accounting bases selected and consistently followed by a business enterprise as being, in the opinion of the management, appropriate to its circumstances and best suited to present fairly its results and financial position".

The SGPD also deals with the subject of general presentation and disclosure requirements for the consolidated financial statements and for those enterprises still under formation. As for consolidated

financial statements, the SGPD requires that the following items should be disclosed (para 745):

- a. The policy adopted by the holding company in preparing the financial statements of its subsidiaries. This disclosure should be a part of the disclosure of significant accounting policies.
- b. The ratio of the holding company's ownership equity in subsidiaries that are included in the consolidated financial statements.
- c. The ratio of the holding company's ownership equity in subsidiaries that are not included in the consolidated financial statements.
- d. The basis of accounting for subsidiaries that are not included in the consolidated financial statements.

Again it should be pointed out that the SGPD does not explain what is meant by consolidated financial statements, holding or subsidiary company, procedures, methods, and accounting terminology used in preparing such statements. It is confined only to general presentation and disclosure.

9.4.4 Auditing Standards

Until very recently, there was no official pronouncement on the subject of auditing standards in Saudi Arabia, although the Companies Law required the financial statements presented to the shareholders in the annual general meeting to be audited by external auditor(s). In the past, auditors in Saudi Arabia have mainly depended upon their own personal knowledge and experience when determining whether or not the financial statements present fairly the financial position of the company concerned. There has been no standardised format

for the auditor's report, so the result has been a variety of reports in different forms (see chapter 5).

As mentioned earlier, the second volume of the first report of the accounting development programme is concerned with auditing standards. Seven standards have been produced so far, classified into three broad categories: General standards, standards of field work, and standards of reporting (Auditing Standards, 1986, para 118). The main features of these standards may be outlined below.

9.4.4.1 General Standards

These standards are concerned with the basic principles which govern the professional characteristics of the auditor in terms of his competence, independence, and the need to exercise due professional care when he performs the auditing procedures. Accordingly, this group consists of three standards as follows (para 119):

A) Standard of Adequate Professional Competence

According to this standard, the auditor and his team should have adequate education and technical training in accounting and related areas to enable them to perform the audit task properly. The standard requires the auditor, before accepting an engagement, to evaluate his professional competence, as well as that of his technical team, to determine whether it is possible for him to carry out the auditing procedures efficiently.

B) Standard of Neutrality and Independence

This standard requires the auditor and his team to be fully independent in all audit procedures. In addition, the standard states that the auditor shall not give an opinion on the financial statements of an enterprise if he discovers, after his appointment, that he or his team is not fully independent with respect to an enterprise in question.

C) Standard of Due Professional Care

This standard imposes several requirements on the auditor. First, the auditor should observe the application of auditing standards in all stages of the audit. Secondly, the auditor should be aware of an enterprise's affairs, circumstances, plans, potential utilization of its financial statements and his report thereof. Finally, the standard requires the auditor to seek the advice of other auditors if the circumstances of the audit make this advisable.

9.4.4.2 Field Work Standards

These standards are concerned with basic principles which govern the establishment of an adequate basis for giving an opinion on the financial statements. This group consists of three standards as follows (para 120):

A) Standard of Planning

This standard requires the audit procedures to be adequately planned in advance and assistants, if any, to be properly supervised. More specifically, the standard

requires the auditor to observe the following (Auditing Standards, 1986, p.29):

1. To select suitable audit procedures in order to obtain adequate evidence to be used as a basis to formulate an opinion regarding the financial statements in question.
2. To plan his work to ensure that all auditing procedures carried out by the auditor's assistants are performed by individuals who have adequate and relevant skills and experience; and under adequate supervision.
3. To ensure that the audit procedures are carried out in accordance with generally accepted auditing standards, and in accordance with any other statutory requirements concerning the implementation of an audit.

B) Standard of Control and Documentation

This standard requires the auditor to direct and supervise all members of the audit team to ensure that audit procedures are performed in accordance with generally accepted auditing standards and any other related statutory requirements. It also requires that all working papers are complete, well organised and ready for any reference which may be needed.

C) Standard of Auditing Evidences

This standard is the longest one as it consists of nineteen articles. In general the standard divides the audit evidences into three parts, as follows: the first is concerned with study and evaluation of the entity's systems, particularly the accounting system and the internal control system; the second is concerned with the analysis of audit samples; and third is concerned with the examination of balances and transaction enquiries.

9.4.4.3 Standards of Reporting

Only one standard comes under this heading. This standard concerns the basic principles which govern the contents of the external auditor's report, the form of the report, and the auditor's opinion regarding the financial statements. The standard requires the auditor to express in a separate paragraph, his opinion whether the overall financial statements present fairly the financial position of an enterprise at the end of the accounting period, the results of its operations, and the application of its funds during the period in question. In addition, the auditor shall state in his report whether the financial statements are prepared in accordance with generally accepted accounting principles suitable for the circumstances of an enterprise under examination.

According to the ministerial decision No. 699 dated 28/2/1406H. (1986), the above auditing standards are considered an official reference to be used as a guide by all Certified Public Accountants practising in the Kingdom of Saudi Arabia.

It must be mentioned, however, that a close look at these standards reveals that they are similar, in their basic context, to those produced by the American Institute of Certified Public Accountant (AICPA) except that they are arranged in seven instead of ten standards. Although the standards contain much detail, particularly the standard of audit evidence, little attention is paid

to the evaluation of the system of internal control of an enterprise under examination, in spite of its importance.

9.5 Evaluation of the Accounting Standardisation Programme in Saudi Arabia

Undoubtedly, a move has taken place toward the advancement of accounting in Saudi Arabia. However, this move is far from being comprehensive and the efforts so far have been confined to the development of accounting and auditing standards for external financial reporting. It should be pointed out that any move to develop accounting in Saudi Arabia should tackle the problems of all components of the accounting system (education, profession, enterprise, government, and national). This is because of the interrelationships among these components, and because the problems in a particular component come not only from within, but also are the result of problems from other components. It has also been argued that "the solution of a problem within one component may cause more problems for another component, or individual solutions within a component may be obviated by the action of another component" (Holzer and Chandler, 1981).

It would seem that Saudi Arabia has chosen flexible accounting when setting accounting and auditing standards for external financial reporting. However, this approach is very complex and can only be operated by sophisticated accountants. This fact was emphasised by Murray (1981, p.18) when stated:

"A complex system of standards can only be operated when there is a sophisticated audience of accountants to implement them."

An analysis of the accounting guidelines published so far in Saudi Arabia reveals that they closely resemble those of the UK and the USA with a bias toward the latter. Perhaps this may be attributable to the fact that most members of the team involved in the project were American professionals and academics and even the Saudi professors (three members) among the team had received their higher education in the USA (see the *Analytical Study*, 1986, pp.139-143).

To improve an existing accounting system or to establish a new one is not an easy task and certainly there is nothing wrong with seeking the *assistance of* accounting experts from developed countries such as the UK and the USA. However, such foreign assistance may result in transmission of accounting principles and practices from the developed countries, which may be unsuitable to the new environment. Perhaps this is what has happened, to some extent, in the recent development of accounting in Saudi Arabia.

In the statement on the objectives of accounting in Saudi Arabia, particular emphasis was placed upon the needs of investors (shareholders) and creditors. Although the statement mentioned various governmental agencies, particularly those responsible for legislation, planning, controlling and directing the national economy, among the users of financial statements prepared by an enterprise,

it failed to specify the type of accounting information needed by them, merely saying that such agencies have the ability to determine the information that should be presented to them by an enterprise to meet their needs (para 53). This means that further efforts need to be made in order to ensure that the appropriate information is prepared for government use.

In addition, shareholders and creditors are ranked at the top of the list of users of financial statements prepared by an enterprise. Although this assumption may seem acceptable in theory, it is not borne out in practice. There is no mention, even in the **Analytical Study** attached to the statement, of how these users were identified and ranked in order. The statement also mentions that positive cash flow is the main source of information for external users, but there is much doubt as to the extent to which these users are capable of understanding and of using published information for decision-making.

Recent evidence suggests that the number of private shareholders in Saudi Arabia has declined; and that external audit reports are neither read nor understood.

"...the number of shareholders has been declining recently in a number of Saudi corporations and shares have become more concentrated in the hands of small groups of investors. For example, the number of shareholders of Saudi American Bank declined from 102,000 to 45,000 shareholders, and in the Arab National Bank the number of shareholders declined 28,000 to 8900 shareholders. ... [in addition] a number of shareholders who received

the company annual reports which includes financial report are unable to understand the basic contents of the report and accordingly no longer participate effectively in the general annual meeting of the shareholders". (AL-YAMAMAH, March 1989, p.47).

As a quick solution to some of the above problems and to assist private shareholders, it has been suggested that the Chamber of Commerce and Industry should prepare and publish a simple booklet entitled "How to read financial reports" (Ibid.).

Further evidence of the lack of sophistication and interests of shareholders in Saudi Arabia, is provided by the findings that in seven Saudi corporations alone, more than SR 158 million subscription surplus and share profits remained uncollected by shareholders. Carelessness and long procedures are said to be the main reasons (AL-YAMAMAH, Nov. 1989, p.47).

Indeed, even if we accept that the groups set out in the recent statement of accounting objectives (para 53) use and properly understand published *financial reports*, they still represent a very small part of the overall objectives of accounting as a tool for economic decision-making. Considering the unique rapid economic development which has taken place in almost all sectors in Saudi Arabia in recent years and the dominant role of the government in planning, controlling and directing the overall economy, accounting should extend its objectives to provide information for users in both public and private sectors at both micro and macro level rather than

concentrating on a certain group of users. As Briston (1981b, p.62) has argued:

"the process of reporting annually to a group of uninterested shareholders who often do not understand the information provided, and could not benefit from it even if they did, is only a small part of the subject of accounting, which already attracts far more attention than it deserves, ... The subject of financial reporting standards should be seen as only a small part of the overall accounting system - a system which involves the collection, processing and communication of information for making, implementing and controlling economic decisions in both the public and the private sector at both the micro and the macro level"

Belkaoui (1988, p.193) pointed out that in most developing countries, the public sector is larger than the private sector and requires different data for economic decisions than those provided by accounting standards of the private sector. As a result, the developing countries need an accounting system suited to their historical, political, economic, and social condition.

Furthermore, Professor Lee (1987, p.7) expresses ^{his} his concern about the accounting standards and the role of external financial reporting in recent years. He argues:

"Apart from an increased complexity in disclosure, the external financial reporting function of late 1980s appears to be little different from that of the 1960s. Indeed, it can be argued in many respects it has not changed substantially since the mid 1860s except for the issue of the extent of disclosure. Thus, accounting standardisation does not appear in its present form to be a catalyst for change. Instead, it appears to

assist in the petrification of financial reporting."

It is thus clear that before going further in this direction and establishing more standards for external financial reporting, which are neither read nor understood, it is necessary to determine what type of accounting information is actually needed in both public and private sectors at micro and macro levels in Saudi Arabia. Having determined this, it would then be possible to consider which type of accounting system would most effectively provide that information for the ultimate users. For example, would this information best be reported by a diversified accounting system based on Anglo-Saxon accounting, or by a national uniform accounting system? It has been argued that it is quite possible that a standardised system such as the French *plan comptable* might be more suitable than Anglo-Saxon accounting for developing countries with few listed companies, sophisticated shareholders or highly qualified accountants (Briston, 1978).

The researcher strongly believes that external financial reporting standards established along the American and the British line are unsuitable for an environment such as Saudi Arabia, where the entire country's economy is planned, controlled and directed by the government, which should therefore be seen as the primary user of such reports. The view that shareholders and creditors are the main users of financial reporting

in the UK and the US is out of touch with present reality in those countries let alone in Saudi Arabia.

It may, perhaps, be added that the problem does not end with producing a set of standards for financial reporting, since these standards need to be implemented, followed-up, reviewed and amended or, in some cases, abolished altogether². Such a task can only be carried out by professional bodies, as is quite clear from the experience of the Anglo-Saxon countries. In the UK, for example, the debate on accounting for changing prices consumed the larger part of the ASC's energies from the publication of the first exposure draft (ED8) in 1973 to that of the standard on the subject (SSAP16) in 1980, and eventual withdrawal of SSAP16 in 1986.

Although throughout the **Analytical Study** attached to the accounting and auditing standards published so far, reference has been made to the Saudi Institute of Certified Public Accountants (SICPA) which is expected to monitor and follow up the implementation of these standards, no such institute has yet been established, and there is no indication of its establishment in the near future. The role of the Ministry of Commerce in monitoring and following up the implementation of these standards undoubtedly would be much more difficult in the absence of accounting experts.

² According to an interview with Mr. Al-Rashed (December, 1989), after the end of the second stage of the accounting development programme (i.e the determination of the accounting objectives and concepts), the proposal to set 44 standards was sent to the Ministry of Commerce. However, this proposal stil under the Ministry consideration and the only information available about it is that the number of standards to be established is reduced to 30.

9.6 Summary and Conclusion

The main purpose of this chapter has been to review and evaluate the recent accounting developments in Saudi Arabia with particular emphasis upon the contents of the accounting and auditing guidelines published so far in order to find out to what extent they meet the socio-economic development needs of the country.

It was shown that a move has taken place for the first time toward the advancement of accounting in Saudi Arabia. However, this move is far from being comprehensive and the efforts so far have recognised only the deficiencies of the accounting profession and finished with the development of accounting and auditing guidelines for external financial reporting. For example, no attention is given to the deficiencies of other components such as accounting education, enterprise accounting, government accounting and national accounting in these recent developments. Moreover, review of the contents of the guidelines published so far in Saudi Arabia revealed that they closely resemble those of the UK and US, placing similar emphasis upon the needs of private shareholders and creditors.

It was argued that in Saudi Arabia, setting standards for external financial reporting along Anglo-Saxon lines seems to be a very complex process at this stage and unlikely to satisfy the current socio-economic development needs of the country. More specifically, Saudi Arabia needs an accounting system which provides information relevant to its socio-economic planning

rather than one which is designed to furnish information to the stock market and its decreasing and uninterested body of shareholders.

CHAPTER 10

SOCIO-ECONOMIC DEVELOPMENT NEEDS AND A PLAN FOR IMPROVING ACCOUNTING IN SAUDI ARABIA

10.1 Introduction

Accountancy nowadays is more and more conceived as an information system within its socio-economic environment, geared towards the decision-making of economic entities. It deals with the identification of economic phenomena, and the analysis, selection, measurement, evaluation, verification and communication of the data in the form of "costs" and "benefits" (Enthoven, 1975, p.4).

Accounting information has little value unless it is relevant to its environment. Saudi Arabia is a developing country which has adopted a comprehensive development planning approach as its vehicle towards growth and socio-economic development. The success of development planning in Saudi Arabia is dependent on the availability of reliable information to those government agencies responsible for planning and directing the national economy.

The purpose of this chapter, therefore, is to discuss the accounting information needs of socio-economic development planning in Saudi Arabia. As the Saudi Arabian economy is entirely based upon a series of five-year development plans, most of the discussion in this chapter will be devoted to the accounting information needed to formulate and control these plans. Moreover, the requirements of other economic development

aspects such as development projects and Specialized Credit Institutions (SCIs) will also be considered. This chapter also discusses the uniform accounting system as an alternative to accounting diversity and shows how, if adopted, uniformity could facilitate the flow of accounting information from various economic sectors to the ultimate users. A proposed plan for improving accounting in Saudi Arabia is presented and discussed in the last section of this chapter.

To gain more insight into the planning process and to determine the role of accounting in the formulation and control of national development plans, an interview was arranged with Mr. Al-Hakmi, Deputy Assistant to the Minister of Planning, at the Ministry of Planning. Much of the information in this chapter is based on this interview and on the official materials provided by him during the course of the interview.¹

10.2 Socio-economic Development Planning in Saudi Arabia

10.2.1 Definition of Development Planning

Various definitions of development planning have been found in the literature. For example, Enthoven (1973, p.149) defined it as "the preparatory evaluation and decision making process of a forward-looking character for an economy, in which alternatives have to be measured, weighed and outlined, and priorities for the use of resources established."

¹ These Materials include: The Planning Manual for the Fifth Development Plan (1990-95); the Plan Document itself; and the Achievement of Planning, Facts and Figures.

Todaro (1985, p.464) described economic development planning as "a deliberate governmental attempt to coordinate economic decision-making over the long run to influence, direct, and in some cases even control the level and growth of a nation's principal economic variables (income, consumption, employment, investment, saving, exports, imports, etc.) in order to achieve a predetermined set of development objectives."

Colm (1968, p.5) stated that it is important to realize that planning is more than the mere preparation of a plan; it should be considered as a system of decision-making under conditions of uncertainty which requires a mechanism for adapting the plan to unexpected developments. Accordingly, *the main elements of a planning system are* (Colm, 1968, pp.5-6):

"(1) the setting of policy, (2) developing programs and projects for moving toward the goals within a specific period of time, (3) designing policies for mobilizing resources (e.g, manpower, taxes, domestic and foreign borrowing) required for the programs and projects, (4) providing information about the progress made and the obstacles encountered in the execution of the programs and projects, (5) providing a mechanism for adopting policies designed to overcome obstacles and to adjust the plan to errors when they become apparent, if necessary by modifying the current plan, and (6) preparing for a subsequent plan."

The Ministry of Planning in Saudi Arabia attempts to integrate some of the above elements and defines the plan as "a set of mutually consistent and integrated courses and programs of action designed to achieve specified

objectives by attaining well-defined targets over a specified period of time, and within calculated human, material and financial constraints" (Planning Manual for 5DP, 1990-95, p.7).

10.2.2 Reasons for Development Planning in Saudi Arabia

Generally speaking, development planning has been adopted by most developing countries due to failure of the market to determine the prices of production factors in these countries. This state of affairs was recognised by the UN (1965, p.12) in the following statement:

"The need for using appropriate criteria for selecting projects arose because of the failure of the market mechanism to provide a proper guideline. In less-developed economies, market prices of such factors of production as labor, capital and foreign exchange deviated substantially from their social opportunity costs and were not, therefore, a correct measure of the relative scarcity or abundance of the factor in question."

Besides the market-failure argument, development planning was deemed necessary by the Saudi Government due to the primitive state of the economic infrastructure and the inability of the domestic private sector to take on the development task. That inability was mainly due to the small size of the private sector and the nationwide shortages of human and financial capital (Al-Jasser, 1986).

Thus, a comprehensive economic planning approach has been adopted in Saudi Arabia to achieve four key objectives: first, to provide a long term conceptual

vision to guide development; second, to provide the organisational framework for coordinated development efforts by the private sector and the government, which involves both policy guidelines for the private sector, and the creation, when necessary, of government-owned enterprises or joint ventures between the government and the private sector; third, to allocate public expenditures to achieve structural change as well as provide government services; and fourth, to strengthen the existing management and direction of the economy (Fifth Development Plan, 1990-95, P.10).

10.2.3 The Planning System in Saudi Arabia

The distinctive feature of the Saudi planning system is its philosophy of achieving socio-economic development within the framework of a free market economy based on Islamic values and concepts. The key elements of the planning system include the following (Fifth Development Plan, 1990-95, p.399):

- A) The National Development Strategy (NDS), which outlines the long term objectives and strategic principles for development;
- B) The Five-Year Development Plans, which are prepared in accordance with the national development strategy, and include:
 - 1. the Plan Document, which outlines the objectives, policies and development targets at the national and sector levels for the plan period;
 - 2. the detailed Operation Plans for each public sector agency, which set out the objectives and policies, demand analysis and issues, development programmes

and targets, resources allocation, and implementation schedule for the agency;

3. **Emirate Reports**, which describe the existing socio-economic conditions and identify future development needs;

4. the regulatory and economic framework for the private sector, which provides information on the likely course of development, and government policies that will affect potential business opportunities.

C) The management of the implementation of the Plan, which includes the preparation of annual follow-up reports for the Council of Ministers, and the continuous process of monitoring, evaluating and assessing the Plan's performance in the light of circumstances.

10.3.4 The Process of Development Planning in Saudi Arabia

As stated earlier, since 1970, Saudi Arabia's economy has been based on a series of comprehensive five-year development plans. Development planning in Saudi Arabia is mandatory for all public sector units, while it serves as a guide for private sector units. Thus each unit in the public sector is required to prepare and submit its plan within the framework set by the Ministry of Planning (interview No. 7).

The formulation of the national development plan in Saudi Arabia consists of a series of ongoing activities as follows [Council of Ministers' Resolution No. 693, dated 4-5/7/1389 H. (1969)]:

1. Current economic conditions and resources available in the country are analysed, and the findings and recommendations reported to the Council of Ministers.
2. After the findings and recommendations of the Ministry of Planning and reports filed separately by the Ministry of Finance and National Economy are submitted, the Council of Ministers draws up a development strategy to guide the formulation of the development plan. The Ministry of Planning then circulates the development strategy to other ministries and agencies with instructions and guidelines for the formulation of their plans.
3. Each Ministry and agency, in consultation with the Ministry of Planning, formulates its own plan and submits it to the Ministry of Planning within the time frame specified in the plan preparation schedule.
4. The Ministry of Planning, in consultation with the different Ministries and agencies, reviews and consolidates the plans of all ministries and agencies.
5. The Ministry of Planning submits the Development Plan to the Ministerial Planning Committee (MPC), which consists of several Ministers appointed by the Council of Ministers. The MPC sets the policy direction for implementing the plan.
6. Plan Approval: The MPC submits the overall plan document to the Council of Ministers, headed by the King, for approval.

It should be pointed out, however, that formal modification of the planning process was introduced for the first time in the Fourth Development Plan (1985-90). This modification involved the adoption of a "Programme-Based Expenditure Approach". According to this approach, each ministry and agency is required to adhere to the financial allocation by programme, while simultaneously increasing its flexibility in the management of spending within the individual programme. Moreover, the focus of planning has been shifted from projects to programmes, from the detailed implementation of individual projects to responsibility for managing expenditure priorities and structure, within a sectoral rather than an agency context (5DP, p.401).

10.2.5 The Role of the Ministry of Planning

While all government agencies are involved in the planning process, the key role is assigned to the Ministry of Planning. The Ministry of Planning was one of six Ministries established in 1975 as the Kingdom developed its institutions in response to the new and vital requirements inherent in its rapid socio-economic development. Besides the task of preparing the national development plan which sets the framework for development activity at all levels in the Kingdom, the Ministry of Planning has the overall responsibility for coordinating development activities and managing plan implementation. In doing this the Ministry of Planning undertakes the

following activities (Fifth Development Plan, 1990-95, pp. 403-405):

A) Follow-up and evaluation to:

1. ensure that development programmes and policies effectively achieve and are consistent with the strategic objectives of the plan;
2. evaluate the performance of policies and relevant programmes so as to provide alternative policy options, when appropriate or required;
3. improve the Ministry's input to resource allocation decisions through assessing the effectiveness of existing resource utilization;
4. enhance information available to decision makers to minimize deviations from the Plan and identify the obstacles/constraints to implementation.

B) Coordination between the plan and the annual budgeting process: to ensure that government expenditures conform to the programme structure and priorities of the plan for each agency, and the composition of budget allocations in terms of recurrent and investment expenditures.

C) Periodic plan reviews: to safeguard against unexpected fluctuations in the economic environment and to ensure that the thrust of the development strategy is maintained, the Ministry of Planning will:

1. monitor and review progress in resolving the key issues presented in the plan, and identify critical issues that may emerge as a result of changing conditions;
2. closely monitor and assess the impact on the plan of new developments in the international economic environment and carry out periodic reviews of the economic and social impacts of the development programmes;
3. prepare a comprehensive mid-term review of the Fifth Plan's implementation.

D) Private sector-government consultation and feedback: the achievement of the Fifth Plan's objectives will require increased coordination between the government and the private sector, and the availability of timely and reliable information and analysis on the performance of specific sectors and the economy in general.

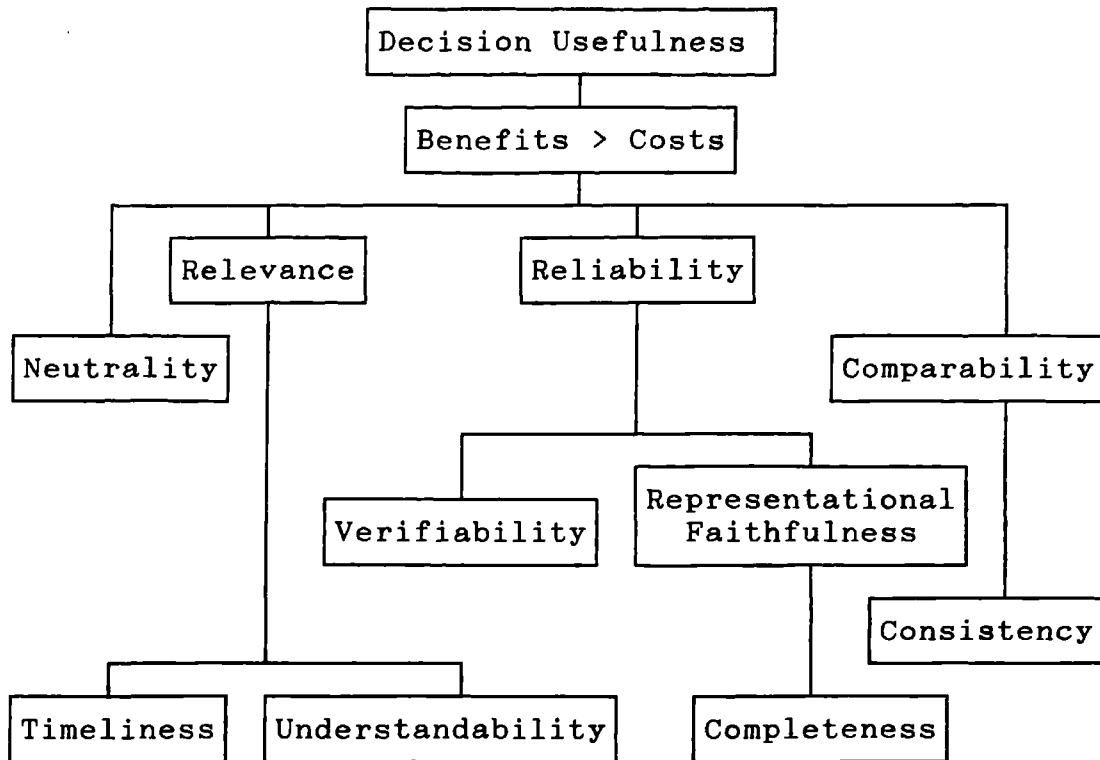
F) Long-term perspectives: to provide a longer term framework to the management of plan implementation and future planning activities, the Ministry of Planning will update long term development perspectives (20 years) for the key social and economic sectors of the economy.

10.3 Accounting Information Needs for Socio-economic Development Planning in Saudi Arabia

10.3.1 Characteristics of Useful Accounting Information

Information has value only when it improves the outcome of the decision in which it is utilized. To be of value, information ought to have certain basic characteristics, which have been identified in various studies. For example, the American Financial Accounting Standards Board in Statement No.2 has specified the characteristics shown in figure 10.1.

Figure 10.1
Hierarchy of Qualitative Characteristics



Source: Financial Accounting Standards Board, Statement of Financial Accounting Concepts, 2 "Qualitative Characteristics of Accounting Information" (Stamford, Conn: FASB, May 1980). in Belkaoui, 1984, p.193

It should be pointed out that the current accounting system in Saudi Arabia is far from producing accounting information with the above characteristics. Indeed, the lack of good quality information and its consequences were recognised recently by the writers of the Fifth Development Plan (1990-95, p.75) when they stated that:

"In many fields of data provision the quality of information produced is not yet up to the standards of accuracy and reliability required for rational and responsible analysis, planning and decision-making. Decisions based on inaccurate information can prove very costly to individuals, organisations and society as a whole."

The inadequacy, both in quantity and quality, of accounting information in Saudi Arabia is attributed to the deficiencies of the current accounting system and its components (see chapters 4 to 8).

10.3.2 Accounting Information Needs for Formulating National Development Plans

An essential element of the formulation of the national development plan is to establish targets for the key elements of the economy. For example, the planners in Saudi Arabia have set a targeted growth rate for Gross Domestic Product (GDP) during the Fifth Development Plan (1990-95) of 3.2 percent per year, with non-oil GDP targeted to grow at an average of 3.6 percent. The production sectors are targeted to grow significantly faster than the overall economy, at an average annual rate of 5.6 percent (see table 10.1).

The formulation of a realistic economic development plan requires that the macro accounting system of an economy generates timely, adequate, relevant and reasonably accurate information about the economic activities of various sectors in that economy. Seidler (1967, p.70) argued that "... detailed statistical data on the performance of the economy and its various sectors are absolutely necessary if the most efficient utilization of available resources is to be accomplished."

Table 10.1
Gross Domestic Product in the Fifth Plan
(in constant 1984/85 prices)

	Value Added (SR billion)		Avg. Annual Growth (Percent)
	1989/90	1994/95	
Production Sectors	88.0	115.9	5.6
Agriculture, Forestry	22.2	31.1	7.0
Other Mining	1.7	2.1	4.0
Manufacturing	33.1	45.4	6.5
Petroleum Refining	17.9	23.3	5.4
Petrochemicals	4.9	7.3	8.0
Other Manufacturing*	10.3	14.8	7.5
Public Utilities	(0.8)	(1.1)	6.9
Construction	31.8	38.4	3.8
Service Sectors	82.8	98.3	3.5
Trade, Restaurants, Hotels	28.2	32.7	3.0
Transport, Communications	21.7	25.3	3.2
Real Estate	9.4	10.8	2.8
Finance, Insurance and Business Services	13.6	18.7	6.6
Community, Social and Personal Services	9.9	10.8	1.7
Government Services	56.2	58.4	0.8
Crude Oil and Natural Gas	122.3	136.6	2.2
Gross Domestic Product	349.3	409.2	3.2

* Value added in 1984/85 price is negative due to operating revenues not covering costs of materials in the base year.

Source: Fifth Development Plan (1990-95), p.85

At this stage of planning, the key figures that must be obtained concern national income, investment, consumption and the balance of payments. The ultimate aim is to determine the percentage of national income that must be invested in order to achieve the target rate of economic growth mentioned above. Most of these figures should to be supplied by the macro accounting system. For example, the national accounts data delineate the structure of the economy and describe some fundamental

economic relationships. In most cases the national product (or national expenditure) data are derived largely from the enterprise statements. Clearly, if the financial accounting data at the business level are inadequate, the macro accounts will also be deficient.

This is exactly the current situation in Saudi Arabia. The lack of sound uniform accounting procedures, and the absence of any linkage between micro and macro accounting contribute much to the distortion of Saudi national income data. Meanwhile, the macro accounting system in Saudi Arabia suffers from technical problems which also contribute to the deficiency of the data (see chapter 8).

In addition to macro accounting information, effective formulation of economic development plans needs more specific measurement tools such as capital-output ratios, input-output tables, and shadow prices. "Capital-output ratios set forth the investment and hence savings required to attain a desired rate of growth in output ..." (Enthoven, 1985, p.9). Input-output tables are "... a deconsolidation and extension of the national income and product," and in that sense, "... they convey detailed inter-industry flows and relationships (Enthoven, 1973, p.90). Shadow prices have been defined by Enthoven (1977, p.29) as:

"the values of the production factors under conditions in which market equilibrium could exist in an economy and investment plans could be executed. These shadow or accounting prices portray society's preference for, and relative

scarcity of, factors of production and constitute an important tool in framing a development plan."

Enthoven (1985, p.10) stated that "without any effort to use shadow prices, wasteful programs or projects might be executed and scarce investment funds misallocated, potentially resulting in less than optimum growth for an economy."

10.3.3 Accounting Information Needs for Controlling National Development Plans

Saudi Arabia needs accounting information not only for formulating national development plans but also to control the implementation of these plans.

In the Saudi Arabian planning system, the overall task of controlling the national plan's implementation is the responsibility of the Ministry of Planning. In order to perform this role the Ministry of Planning needs reliable information from all agencies included in the national plan, giving a systematic analysis of their implementation of the relevant programmes and projects. The agencies must indicate in as much detail as possible, the amounts of expenditure made on every individual project and the stage of development of the project.

The availability of such information on a regular basis will allow the Ministry of Planning to evaluate the effectiveness of policies, improve coordination between the plan and the annual budgeting process, identify plan constraints, and analyse the impacts of these constraints upon the overall implementation of the plan.

10.3.4 Accounting Information Needs for Development Projects

The success of development planning in Saudi Arabia and the achievement of its objectives is dependent, to a large extent, upon the selection and implementation of projects by various economic sectors. This is because each plan consists of a series of projects which require the compilation of information relating to the production of specific goods and services. However, before discussing the function of accounting in the development process it is appropriate to explain what is meant by a project.

The United Nations (1958) has defined a project "as the compilation of data which will enable an appraisal to be made of the economic advantages and disadvantages attendant upon the allocation of a country's resources to the production of the specific goods or services" (Enthoven, 1973, p.171).

The World Bank has interpreted projects to mean proposals for capital investment to develop facilities to provide goods or services (King, 1967, p.3). The investments may consist of the building of entirely new facilities or the expansion or modernization of existing ones. The techniques of project appraisal are equally applicable to the preparation of data and the assessment of projects by private businesses or government agencies in all countries (Ibid., p.4).

The Ministry of Planning in Saudi Arabia has defined the term project as "an individual item of a programme

(or subprogramme) such as a specific hospital within the hospitals construction programme, or a specific activity such as the training of (50 staff) or administrative organisation .. etc." (Planning Manual for 5DP, 1990-95, p.7).

Moreover, the Ministry of Planning has provided the planning units of each industry with some useful guidelines and specific forms concerning the preparation of their projects. According to these guidelines, a distinction has to be made between new projects and ongoing projects. New projects are those which are to be included in the new plan for the first time. Industries subject to this type of project are required to complete and submit to the Ministry of Planning the form shown in figure 10.2. This form has been classified into two main parts. The first part includes the basic information concerning the project in question, such as name of agency in which the project is to be undertaken, name of programme, name of project, project code, location, and the duration of the project. The second part consists of three sections as follows:

- (a) project cost, which includes all expenditure involved in the project;
- (b) total manpower required for implementation of the project; and
- (c) manpower requirements for operation and maintenance.

Figure 10.2 New Project Form

Agency: _____ Budget Number (If ongoing): _____

Sub-Agency: _____ Project under Construction: _____

Name of Main Program: _____ Project Code: _____

Name of Sub-Program: _____ Units of Measure: (See Manual) _____

Name of Project: _____

Name of Sub-Project: _____

Location: (City/Village): _____ Start Year _____ Month _____ End Year _____ Month _____

Emirate:Region

Ongoing/New _____ Study/design _____ Implementation _____ Operation _____

A. Project Cost (in thousands of Saudi Riyala)

Type of Expenditure	Total Estimated Cost of Project		Spent or Committed Until		Planned		PDP Total		Remaining to be spent
	1408	1409/10	1409/10	1411/12	1412/13	1413/14	1414/15		
1. Study/design	_____	_____	_____	_____	_____	_____	_____	_____	_____
2. Land	_____	_____	_____	_____	_____	_____	_____	_____	_____
3. Construction	_____	_____	_____	_____	_____	_____	_____	_____	_____
4. Equipment/Plant	_____	_____	_____	_____	_____	_____	_____	_____	_____
5. Operation	_____	_____	_____	_____	_____	_____	_____	_____	_____
6. Maintenance	_____	_____	_____	_____	_____	_____	_____	_____	_____
7. Training	_____	_____	_____	_____	_____	_____	_____	_____	_____
8. Other (Explain)	_____	_____	_____	_____	_____	_____	_____	_____	_____
9. Total	_____	_____	_____	_____	_____	_____	_____	_____	_____

B. Total manpower requirement, for implementation of projects (Chapter 4): _____ Man-year

C. Manpower Requirements for Operational and Maintenance (Chapter 3)

Type of Manpower	Target						
	1408/09	1409/10	1410/11	1411/12	1412/13	1413/14	1414/15
Management and Administrative Professional	_____	_____	_____	_____	_____	_____	_____
Sub-Professional and Technical Clerical and Related Skilled Workers	_____	_____	_____	_____	_____	_____	_____
Manual and Service Workers	_____	_____	_____	_____	_____	_____	_____
Total	_____	_____	_____	_____	_____	_____	_____

S = Saudi .. SOURCE: Planning Manual for the Fifth Plan (1990-95).

Ongoing projects are those which have already been started and are continuing at the time of the plan's preparation. Industries subject to this type of project are required to complete and submit to the Ministry of Planning the form shown in figure 10.3. This form is also divided into two main parts. The first part is almost the same as that of the previous form. However, the second part is different in that it includes information about the contractor, project duration, percentage of completed work and expected date for completion.

For all projects, whether new or ongoing, it is necessary to state the expected or actual starting dates and expected completion dates. For construction projects, these dates should reflect the study, design and construction periods as indicated.

Each project is to be classified by type code. A listing of project type codes and associated units of measure should be entered in the spaces provided. These codes and units of measure are supplied by the Ministry of Planning (Al-Hakmi, Dec. 1989).

Figure 10.3 Ongoing Project Form

Agency: _____

Sub Agency: _____

Project Code: _____

Sub-Project Code: _____

Name of the Project: _____

Total Cost: _____

Approved Amount: _____

Name of the Sub-Project: _____

Year of Approval: _____

Fiscal Year: _____

Number of Contracts Signed: _____

S. No.	Name of Contract*	Type**	Name	Contractor		Total Value of contract	Actual Spent amount of contract value	Information on Project Duration				Location (City/Village)	Percentage of Completed works	Expected date for completion
				Nation-ality				Date of Award	Date of Signing the contract	Date of Site hand-over	Period in months			
1.	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____
2.	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____
3.	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____
4.	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____
5.	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____
6.	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____
7.	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____
8.	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____
9.	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____
10.	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____
11.	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____

* List the contracts signed within one project.

** Construction, Operation, Maintenance, Supervision etc. Source: Planning Manual for the Fifth Plan (1990-95).

Table 10.2: Code and Type of Project

Code	Type of Project
000 - 099	General Projects
100 - 199	Agriculture Development
200 - 299	Municipal Development
300 - 399	Water and Sewage
400 - 499	Social Development
500 - 549	Defence and Security
550 - 599	Information
600 - 649	Electricity and Energy
650 - 699	Environment Protection
700 - 749	Transport
750 - 799	Telecommunications
800 - 899	Education and Training
900 - 999	Commerce and Industry

Source: Compiled from Planning Manual for Fifth Development Plan, 1990-95, pp.30-75.

At the outset, projects are classified and coded by major sectors - general projects, agricultural projects etc (see table 10.2) - then each individual project comes under a specific sector and is coded accordingly. For example, establishment of a new hospital will be classified under Social Development (400 - 499) and coded as follows:

400 - 499 Social Development

401 Hospital

1. Gross Area in SQ.M.
2. Net Building. Area in SQ.M.
3. Net In-Patient Area, in SQ.M.
4. Net Out-Patient Area, in SQ.M.

5. Net Non-Patient Area, in SQ.M.
6. Number of Beds
7. Type of Hospital
 - A. General
 - B. Specialist
 - C. Endemic
 - D. University
8. Project Type
 - A. Construction
 - B. Operation
 - C. Maintenance

In the case of complex projects, such as airport construction, it will be necessary to disaggregate the project into similar types of subprojects, such as terminals, pavements, etc., and show starting and completion dates, units of measure, and project type code, etc., for each sub-project. This information, with other supporting information, will be used by the Ministry of Planning to estimate the physical and financial resources the project will require (interview No. 7).

However, whether the project is small or large, it is considered as a part of the economic plan and thus the feasibility and justifiability of such project must be appraised before it is integrated into the plan. The accounting function can help, not only in supplying information useful in formulating and controlling the economic development plan, but also in the process of project appraisal. The project appraisal covers all assessments related to a "project cycle". The project cycle runs through three main phases - identification and formulation, evaluation and selection, and execution and follow-up - and accounting is expected to play an important role in each of these phases.

Firstly, the identification and formulation phase: the objective of this phase is to determine whether a potential project and the sector in which it falls are of economic priority to the development of the country; and whether the project appears feasible and viable to implement, carry on and administer. This will require studies to be undertaken concerning the country's available resources, the cost factors involved in production, the expected return and other indirect effects. These studies will need *accounting information* such as preliminary costs and benefits, comprehensive data on materials, labour, capital, overhead costs, potential sales revenue, expected behaviour of various costs and revenues in the future as well as the possibilities of savings in foreign exchange due to a given project (Enthoven, 1973, p.172-73).

Secondly, the project evaluation and selection phase: the objective of this phase is to select from the group of projects identified in the first phase, the project or projects which should be carried out, based on their cost and benefit analysis. Projects with greater net benefits should be given priority of execution. The function of accounting at this phase is to make specific cost measurements and to ascertain that relevant items are incorporated in the decision model (Ibid. p.175).

Thirdly, the project execution and follow-up phase: the objective of this phase is to calculate the actual costs and benefits of the project and to compare them

with those costs and benefits calculated in the first two phases so that feedback and control is possible. Thus, periodic information concerning total actual costs incurred to date as a percentage of estimated total costs of the development projects is needed so it can be related to the percentage of the works completed, in order to determine whether the unused allocated funds are enough to carry out the work needed to complete the projects. Such information is very important for financial planning purposes because if additional funds are needed to complete the projects, these can be raised in time. Alternatively, if the remaining allocated funds are more than enough to pay for the work to be completed, the surplus funds can be saved to finance other developmental activities.

It should be pointed out, however, that under Saudi Arabian practices, there are no comprehensive rules for project appraisal, but only the general guidelines mentioned earlier in this section. Project appraisal can be based on different criteria. Some projects, even though they are not economically viable, may be selected in accordance with government policy. Moreover, project appraisal in the private sector is even less satisfactory. A recent report shows that a number of enterprises have gone bankrupt because they were established on an ad hoc basis and without accurate feasibility studies (Al-Khamees, 1991, p.48).

It is therefore quite clear that project appraisal should be given more attention by both the public and private sectors if the overall plan is to accomplish its objectives. There is no doubt that the ultimate success of project appraisal in Saudi Arabia is dependent on a better accounting system, which can generate relevant, accurate and timely cost and financial accounting information. Because project appraisal in development planning rests to a large extent on the use of cost-benefit analysis, the next section discusses this technique. The purpose of this discussion is to demonstrate the need for accounting information in project analysis and evaluation.

10.3.5 The Need for Cost-Benefit Analysis

Cost-benefit analysis is a technique used to evaluate the desirability of a number of projects which have varying terms. The costs and benefits of each project should be compared with each other at the same point of time. Belkaoui (1988, p.195) stated that "the main objective of cost benefit analysis is to determine whether a particular expenditure is economically and socially justifiable."

The preliminary step in CBA is the definition of the project under consideration. Once this is accomplished, the analyst can proceed to enumerate the costs incurred and benefits generated over the life of the project. Enumeration of the benefits can be divided into two categories: direct and indirect. Direct benefits of the

project are those benefits which accrue directly to the users of the service provided by the project. Indirect benefits are those benefits accruing to entities other than the users of the service provided by the project (Ibid, p.196). For example, in the case of constructing a fast motorway, the direct benefits will be improved traffic-flow and reduced accidents for the users of such a motorway, while the indirect benefits might be the increased rental value of sites, filling stations and restaurants near such a motorway. In enumerating benefits, only the real increase in output should be considered. Any increase in the value of existing assets is not considered a benefit for a particular project (Prest and Turvey, 1965, p.708).

Direct costs of a given project are those incurred directly by the users of the goods or services provided by the project. In the case of the motorway they include capital costs, operating and maintenance costs, and personnel expenses. Indirect costs are those incurred by those other than the users of the goods and services provided by the project.

In enumerating costs, it is necessary to reflect carefully on the alternatives forgone as a result of choosing a particular project, since listing direct resources costs provides only a partial account of actual costs. All external costs must be considered. For example, the construction of a motorway will displace

land that would otherwise be available to farmers, wildlife, country ramblers etc.

Having specified the various costs and benefits, the next step in the CBA is discounting the costs and benefits which are expected to occur. There are three possible investment or decision criteria and the choice of an appropriate discount rate is of crucial importance. The three alternative methods are: the net present value, the ratio of the present value of benefits to present value of costs and the internal rate of return.

Under CBA the decision criterion is that a project should be undertaken providing that the discounted value of social benefits attributed to the project exceeds the discounted value of social costs attributed to the project.

10.3.6 Accounting Information Needs for Specialized Credit Institutions (SCIs)

The inability of the private banking sector to provide term credits to finance private development projects led the Saudi Government to establish six specialized credit institutions. These institutions and their main objectives are as follows:

1. The Saudi Agricultural Bank (SAB) was established in 1962 to provide loans and credit facilities for the development of agriculture-related activities.
2. The Public Investment Fund (PIF) was established in 1971 to provide medium and long-term finance for local organisations such as the General Petroleum and

Minerals Organisation (Petromin), SAUDIA (Saudi Arabian Airline) and other domestic industrial enterprises.

3. The Real Estate Development Fund (REDF) was established in 1974 to provide loans to individuals and companies for private or commercial real estate projects, of up to 70 percent of construction costs.
4. The Saudi Credit Bank (SCB) was established in 1974 to provide interest-free loans to low income Saudi nationals for specified socio-economic purposes.
5. The Saudi Industrial Development Fund (SIDF) was established in 1974 to provide support for industrial (mainly electricity) companies, lending up to 50 percent finance for ventures which are at least 25 percent Saudi-owned.
6. The Special Credit Programme (SCP) was established in 1974 to provide interest-free loans to Saudi contractors to finance direct purchase of required materials, and credit facilities for short or medium-term loans.

According to the Fifth Development Plan (1990-95), the total assets of these institutions amounted to SR 197 billion in 1988/89, and since their inception, loans have exceeded SR 234 billion (see table 10.3). Moreover, the SCIs are targeted to lend around SR 37 billion during the fifth plan period (1990-95).

Table 10.3
Specialized Credit Institution Loans:
Cumulative Value to the end of 1988/89

Institutions	Value (SR billion)	Share (%)
Real Estate Development Fund	91.7	39
Public Investment Fund	63.5	27
Saudi Industrial Development Bank	49.4	21
Saudi Arabian Agricultural Bank	22.8	10
Saudi Credit Bank	3.0	1
Special Credit Programmes	3.7	2
Total	234.1	100

Source: Fifth Development Plan (1990-95), p.162

The above institutions receive their capital and lending resources from the general budget of the State. The monetary return is not the only basis for government investment or granting of loans to enterprises. Other government objectives include manufacturing, manpower development, and the balanced distribution of economic activity in the country. This indicates that the government is directly concerned with the success of these enterprises in achieving objectives that may not be subject to financial accounting measurement. The government is also directly concerned to know the ability of these enterprises to grow and progress. Thus, the government needs regular and up-to-date information (both financial and non-financial) to assess the effectiveness of enterprises in which an investment is made or to which a loan is given, in achieving their objectives.

10.4 Accounting Uniformity and Socio-economic Development Needs of Saudi Arabia

As stated in the previous chapter, Saudi Arabia appears to be moving towards the adoption of a flexible accounting approach by establishing accounting and auditing standards for external financial reporting similar to those of the UK and the USA. It was also pointed out that the main feature of this approach is the availability of a wide choice of accounting methods. For many transactions, accountants are able to choose from a selection of accounting methods, each of which is equally acceptable, but which often give widely different results.

Furthermore, this type of accounting system is concentrated mainly upon the needs of external users of financial statements, while the needs of government and management are totally ignored (Briston, 1978). Moreover, the implementation of such a system requires a very sophisticated accounting audience, which is hardly to be found, at least for the time being, in Saudi Arabia.

The purpose of this section is to highlight the main features of the uniform accounting system, to address the question of how the uniform accounting system might help to meet the socio-economic development planning needs of Saudi Arabia, and to discuss the experience of other countries operating such a system.

10.4.1 Definition of Uniformity

Accounting literature gives various definitions of uniformity. For example, Mueller (1967, p.93) stated that "uniform accounting means the uniform treatment of all accounting methods, procedures, and concepts ... It includes standardization of valuation applicable to accounting and specified treatment of accountable events like business combinations, inceptions of private pension plans, or receipt of governmental subsidies or tax concessions."

Samuels and Piper (1985, p.56) defined uniformity as "a condition in which everything is regular, homogeneous or unvarying. It implies sameness, and in this context means that all accounting principles and practices are the same."

Alhashim (1985, p.6) associated uniformity with purpose and defined it as "a system of accounting control in which the interpretation of economic events and the prescription of accounting methods, standards, and reports are responsive to definitive user needs."

Uniformity thus can be seen as a way of establishing a consistent body of accounting rules and accounts terminology applicable to multi-purpose accounting systems; and the main function of accountants and auditors under such a system is compliance with these rules and terminology.

10.4.2 Types of Uniformity

Various types of accounting uniformity exist in practice, ranging from application of uniform accounting standards and rules to a comprehensive uniform accounting system. Enthoven (1973, p.223) identified three levels of uniformity, as follows:

(1) The uniform application of accounting standards, practices and convention.

This type of uniformity involves acceptance of accounting and auditing concepts, principles, rules, and reporting procedures, for examples, the allocation and valuation of fixed assets, inventories and research costs and other expenses. This type of uniformity is considered as the weakest of all, because the degree of uniformity here is limited.

(2) The uniform chart or frame of accounts.

This type of uniformity is primarily concerned with specifying classification categories either for all economic units, or by specific sectors and industries, on a domestic, regional or international scale. Basically, it reflects a more standardized layout of accounts and the procedures for classification and allocation of data. This type of uniformity is generally micro-oriented and is used in various countries, mainly for specific industries, such as public utilities, canning, airlines, railways; it facilitates business analysis and evaluation. The Swedish "M-Chart" might be cited as an example of this type of uniformity.

(3) The uniform plan of accounts.

This type of uniformity is macro-economic in orientation. It comprises not only the classification chart but also identification, collection, measurement, processing and reporting of data. The system can be very rigid or very flexible in its degree of uniformity, and may be compulsory or voluntary. Such a system is presently exercised in Russia, France, Egypt, Iraq and a number of African countries which were formerly French colonies.

10.4.3 Reasons for Uniformity in Accounting

Accounting development based on a pattern of uniformity in accounting has long intrigued scholars and others concerned with accounting information. Mueller (1967, pp. 88-92) gave five main reasons for this:

1. The long quest to make accounting more scientific. This calls for a change in accounting from a state of a relatively slow pace of pragmatism to a state of adaptation to the environment.

2. The use of accounting as an administrative device by government as well as business. Governments can use it as a tool for economic and business control. This is more so when governments take full control of business activities and tend to run an entire economy as if it were a giant business firm. For this purpose they require that all accounting inputs have the same basis and character, all accounting information be strictly

comparable, and all accounting outputs be uniform in all respects.

3. Relative simplicity in recording and classifying financial data, and manipulating the data for the purposes of financial reports.

4. For tax purposes, a degree of uniformity is almost a necessity. Whether an income, property, sales, or other tax is involved, the fairness of assessment depends on the degree of uniformity and the reliability of the financial data.

5. The uniformity of data collection facilitates the collection of national statistics, particularly national income statistics.

Uniformity in accounting systems has found support amongst theorists and governments, with the latter group providing practical examples of its application. The most rigid and widespread form of uniform accounting system in existence is that found in the former Soviet Union, where it is applied for development planning and control purposes (Campbell, 1963; Mills & Brown, 1966; and Gorelik, 1973, and 1974). Other countries have adopted uniform accounting systems for similar macro-economic reasons, for example, Nazi Germany (Abel, 1971), Peru (Radebaugh, 1975), and Egypt (Briston and El-Askher, 1984).

It should be pointed out, however, that there are several barriers to the uniform accounting system, which include, among other things, strong accounting

professional bodies and the private industrial accountants. For example, strong accounting professional bodies, such as exist in the UK and USA, are likely to resist any move toward the establishment and implementation of a uniform accounting system, for fear that their independence may be curbed. However, in many developing countries, such as Saudi Arabia, there is no accounting professional body and the private industrial accountants are not strong enough to resist the establishment and implementation of a uniform accounting system.

10.4.4 Arguments For and Against Uniformity

There are several arguments used to support the case for greater uniformity of accounting method.

1. **Better comparability:** the most important argument is that uniformity of accounting procedures will allow comparisons of accounting reports. Similar situations will be reported in a similar way and results will be directly comparable.

2. **Ease of operation:** many accountants claim that increased uniformity would make their job much easier. Choosing an accounting procedure is, for many accountants, time-consuming, difficult and contentious. It may lead to conflict between management, which wants creative accounting, and accountants who believe that another method is more appropriate. With uniformity, the chance of conflict over accounting method would be reduced.

3. **Legal aspect:** under uniformity, accountants would be better able to defend their procedures in court. Because their choices would be limited, they could not be accused of choosing an accounting method to meet the needs of any particular group (Henderson and Pierson, 1980, p.103).

4. **Consolidation and integration of data:** it is argued that under uniformity, collection and integration of data at corporate, sectoral, national and even international level would be facilitated (Enthoven, 1973, p.236).

On the other hand, however, there are several arguments raised against uniform accounting. The following are perhaps the most important (Enthoven, 1973, p.237; Henderson and Pierson, 1980, p.104):

1) **Unreal comparability:** forcing enterprises to use uniform accounting procedures in different contexts will not necessarily lead to comparable accounting reports.

2) **Hindering management freedom:** uniformity would infringe upon the basic rights and freedom of management. It is claimed that management should be left free to select among accounting alternatives in accordance with the needs of the economic situation.

3) **Reduction of professional judgement:** Many accountants fear that to substitute the prevailing guidelines with enforceable rules would reduce their professional status and leave them as mere clerks, interpreting rule books.

4) Preventing the development of a dynamic accounting theory: Uniformity would place accounting in a straitjacket of rules and procedures which would stultify the development of accounting theory and practice. Opponents claim that a large body of rules and procedures would become fossilized, and change and improvement would be stifled. However, evidence has shown that uniformity has helped speed the development of sound accounting practices (Holzer and Tremblay, 1973).

5) Heavy cost: Opponents of uniformity argue that the design of a complete uniform accounting system, which would detail explicitly the ways of applying every single accounting principle, method, procedure, classification and policy would be a very costly process for firms, especially smaller ones.

However, the argument concerning the cost of uniformity may not be valid, as there is ample evidence to suggest that a flexible accounting system can lead to high expenses, whether in observing management preference or in operating to minimize costs caused by management's freedom of choice among accounting alternatives. It is also argued that the audit fees would be greater under a flexible system than under uniformity system. For example, Briston (1990, p.216) pointed out that in the United Kingdom, which operates flexible accounting model, this results in the publication of one million sets of audited accounts each year at a cost of £1000 million. Moreover, costs would be borne in terms of setting

accounting standards for external financial reporting under the flexible system. For example, the costs of the new system of standard-setting in the UK are estimated to be more than 1.5 million pounds annually.

Despite the arguments raised against uniformity, it is believed that in view of the requirements of the economic process, the advantages to be derived from more uniform accounting, whether partial or complete, outweigh the disadvantages (Enthoven, 1973, p.238).

10.4.5 How Uniformity Might Facilitate Information Provision for Socio-economic Development Purposes in Saudi Arabia

Uniformity in recording and reporting accounting data generally aims at simplifying and unifying all aspects of accounting for the purpose of improving the reliability and consistency of accounting data. It has been argued that a national uniform plan is a prerequisite for effective planning. Mueller (1967, pp.97-98) stressed this point when he suggested that:

"The importance of uniformly prepared accounting data is acute in a central planning function because (1) any plan is only as good as the data on which it is based and (2) there is a high degree of interdependence among forms and among sectors of an economy when all of their respective activities are governed by a master plan."

Enthoven (1973, p.294) argued that adoption of and adherence to a uniform accounting system in both the private and public sectors of an economy "... would greatly facilitate ecoddev. accounting requirements for

social accounting, development planning, project appraisal, capital formation and government administration." Enthoven (1969, p.25) claimed that the advantages of such a standardized accounting system would be:

"... easier analysis, evaluation and comparability; better studies of feasibility and costs; facilitation of fiscal administration, budgeting, control, and auditing; more reliable social accounts, more unified accountancy theory; and improvements in economic planning and policies."

Bray (1973) pointed out that uniformity is required if accounting is to be of full use to macro-planning, and drew attention to the need for imputation of values to those factors to be used as indicators or principal measures in constructing and interpreting the national plans. For the same purpose, Elliott (1968) mentioned that uniformity in the preparation, presentation, classification and terminology in financial statements should be a goal of Latin American LDCs if accounting was to play a positive role in their economic development.

Briston and El-Ashker (1984, p.134) asserted, with reference to the Egyptian uniform system, that tabulation of data in a unified manner would:

- 1) facilitate the efforts of the nation to collect the desired information;
- 2) ensure an improvement in the accuracy of information;
- 3) shorten the time needed to collect data on all economic activities in the country; and

- 4) enable management to judge its performance through comparisons with similar enterprises.

Indeed, the Ministry of Planning in Saudi Arabia has recognised the advantages of uniformity. For example, the Ministry states in the Planning Manual for the Fifth Development Plan (1990-95, p.12) that "information concerning the development programme proposed for each government agencies should be provided in tabular form. These data must be submitted on a uniform basis by all agencies, so that they can easily be used by the Ministry of Planning staff for analysis."

A large proportion of industry in Saudi Arabia, including all public utilities and major industries such as oil and petrochemical industries, is managed and controlled by the government. In such a situation, uniform accounting can be more efficiently used as a tool to implement specific economic measures, simply because uniform treatment of similar transactions can more closely be supervised and adherence to the desired procedures assured.

Furthermore, in order to achieve the macroeconomic growth targets of the Fifth Plan (1990-95), an estimated total investment of SR 386 billion will be required. The institutional sources of this investment are shown in table 10.4

Table 10.4
Estimates of Investment Financing Requirements by
Sector and Source (SR billion in current prices)

	Total	Gov. Budget	SCIs	Gov. Owned Comps	Private Sector
Production Sectors	129.6	32.4	15.9	16.9	64.4
- Agriculture	18.4	0.9	6.9	---	10.6
- Other Mining	2.6	1.2	---	0.3	1.1
- Manufacturing	54.6	1.3	9.0	13.6	30.7
- Public Utilities	39.2	29.0	---	2.3	7.9
- Construction	14.8	---	---	0.7	14.1
Service Sectors	84.9	22.5	0.6	9.2	52.6
- Trade	23.3	---	---	0.2	23.1
- Transport, Communications	32.2	22.5	0.6	7.2	1.9
- Real Estate	9.7	---	---	0.5	9.2
- Financial and Business Services	13.5	---	---	0.7	12.8
- Community and Personal Services	6.2	---	---	0.6	5.6
Government Services	95.9	95.9	---	---	---
Crude Oil and Natural Gas	30.9	0.2	---	30.7	---
Residential Housing	45.0	---	18.4	---	26.6
Total	386.3	151.0	34.9	56.8	143.6

Source: Fifth Development Plan (1990-95), p.104

According to this table, the government budget is targeted to provide SR 151 billion for investment in transportation facilities, government services (such as schools and hospitals), utilities and other public facilities.

Specialized Credit Institutions (SCIs) are expected to provide nearly SR 35 billion in investment by recycling repayments of outstanding loans.

Government-owned companies are expected to provide about SR 56 billion in investment, mainly from retained profits and depreciation charges.

The private sector is expected to contribute about SR 144 billion of total investment in the Fifth Plan. Financing of this investment will come primarily from retained earnings of private sector companies, private savings, commercial bank loans, and private capital brought from overseas.

It is clear that the government will provide more than 60% of the overall investment required to accomplish the macroeconomic growth targets of the Fifth Plan. The mobilization of these government capital resources to meet the socio-economic needs of the Kingdom requires an effective accounting system which generates regular and up-to-date information (both financial and non-financial). In effect, such information can not be achieved on time and in proper formats, because the current accounting system in Saudi Arabia, including the recent developments, is based on the Anglo-Saxon accounting system, which emphasises the needs of the private shareholders and creditors rather than the government or the public sector. A national uniform accounting system designed with a strong public sector emphasis would be better for providing such information.

Finally, a uniform accounting system has specific advantages for Saudi Arabia because such a system should facilitate the training of accountants for national reporting and so be a factor assisting in reducing the shortage of accountants (Alhashim and Garner, 1973); uniformity in practice should also reduce ambiguity

arising from differences in outcomes which may arise through the diversity of practices permitted under the present system (see chapter 6) and facilitate the understanding of financial statements.

10.4.6 The Current Accounting Environment in Saudi Arabia Needs Uniformity

Alhashim and Garner (1973) identified a set of circumstances and conditions under which uniform accounting may be desirable and acceptable in any country. This issue has been advanced recently by Perera (1989) who argued that because of the special circumstances of developing countries, accounting practices based on the uniform approach may be the only alternative available to them. Perera (1989, pp.150-54) developed seven hypotheses in support of his argument. These hypotheses are discussed with reference to the Saudi Arabian environment to demonstrate how the prevailing environmental circumstances and conditions advocate the adoption of uniform accounting approach in the country.

Hypothesis (1): "The heavier the government's involvement in economic affairs, the greater the need for accounting uniformity."

In Saudi Arabia the growth of the national economy as a whole is guided by a centralised development plan. The plan, which includes a specific set of social objectives and the resources to be employed to achieve those objectives, is prepared by the economics and financial experts of the Ministry of Planning and

approved by the Council of Ministers, headed by the King. Although the implementation of the plan is the task of all government agencies and of the private sector, the management of this task and the coordination of development activities is the responsibility of the Ministry of Planning.

Thus, it can be seen that the government in Saudi Arabia is heavily involved in the country's economic affairs. Indeed, this situation is not unique to Saudi Arabia, but is common in many developing countries. For example, Enthoven (1977) pointed to the usually high degree of influence held by governments over the economies of developing countries and the emphasis given to control and planning. This environmental condition led Enthoven to postulate that the accounting systems of enterprises in developing countries should be linked to the national accounts and external financial statements should be prepared with these macro purposes in mind. This would require greater uniformity, greater use of current rather than historical cost, and the reporting of certain future-oriented information, such as budgets and projections.

Hypothesis (2): "The more urgent the felt need for economic development by a central government, the greater the desirability of uniformity."

It was stated earlier that an urgent need for economic development has been felt by the Saudi government since 1970. Four five-year development plans

have been implemented so far and now the government is half way through the fifth plan. A comprehensive economic planning approach has been adopted by the Saudi government due to the primitive state of the economy infrastructure and the inability of the domestic private sector to take on the development task. The Five-year plans have aimed to achieve balanced economic, social and regional development.

Hypothesis (3): "The lower the level of accounting education in a country in comparison with industrialised countries, the greater the need for uniformity."

Accounting education in Saudi Arabia was discussed in chapter 4 of this study. It was shown that accounting education has not developed enough to keep pace with the increased demand for accounting skills. Adoption of a uniform accounting system would make the job of accountants much easier, for much of their work would be routinized, whereas choosing an accounting method may be time-consuming, difficult and contentious (Perera, 1989)

Hypothesis (4): "The less the availability of trained management, the greater the need for uniformity."

The lack of well-trained personnel is felt in both public and private sectors in Saudi Arabia. As for the public sector, it has been stated that one of the main problems which hampers the prompt preparation and submission of the final accounts of the state is weakness in the technical ability of those dealing with financial affairs in the ministries and public agencies (see

chapter 7). As far as the private sector is concerned, it has been stated (Anastos, Bedos, and Seaman, 1981, p.85) that:

"The Saudi businessman is confronted by an extreme shortage of educated managerial personnel. Thus, the employer is not always able to hire adequately trained individuals. ... the Saudi businessman cannot be as demanding in his hiring standards and must be prepared to accept the fact his new employee may not perform up to expectation."

Indeed, very little has changed since, and the present study shows that the lack of national trained personnel is still one of the most serious problems facing Saudi corporations (see chapter 6).

Given these observations, it can be inferred that managers in both public and private sectors in Saudi Arabia have not been trained adequately. Thus, a uniform accounting system in which these managers can be trained is urgently needed.

Hypothesis (5): "The lower the professional status of accountants, the more important is the reason for uniformity to protect the general society."

It has been argued that if a society accords places to accountants' professional prestige, and if accountants claim that they have a crucial role to play in that society, a considerable degree of tolerance is shown toward diversity in accounting practices. This diversity in accounting practices is accepted by the society since there is a minimum of doubt as to the honesty of these accountants and the role they play in the society.

Accountants in such cases accept this responsibility, and they may set up procedures to monitor the actions of individual practitioners in order to keep the reputation of the profession in high public esteem. However, if there is a doubt as to the accountant's role, and if a society considers accountants as clerks, trusting them little, then accounting uniformity can be easily accepted by the society for its protection (Alhashim and Garner, 1973; Perera, 1989).

The main features of the accounting profession in Saudi Arabia were discussed in detail in chapter 5. It was shown that the accounting profession has not developed sufficiently to keep pace with the rapid economic development which has occurred during the last two decades. Professional accountants still operate without a code of ethics, and there is no professional body which could set national accounting and auditing guidelines and organise professional examinations and training programmes based upon the needs of the local socio-economic environment. Moreover, there is no effective public recognition, other than the enacting of the Law of 1974, and the public in general can hardly distinguish between the terms "accountant" and "cashier".

Hypothesis (6): "The more the members of a society identify their own interests with the interests of society, the greater the acceptability of uniformity."

It was stated earlier that Saudi Arabia is an Islamic State. Its constitution, political system, and

socio-economic development are all based upon Islamic teachings (see chapter 3). In such an environment, the social life of the people is based upon supreme principles and designed to secure the happiness and prosperity of the individual and of society. Indeed, there are many verses of the Qur'an and sayings of the Prophet which emphasize the role of the individual in Islamic society. For example, Allah (God) said in the Holy Qur'an (5: 1-3) "O you who believe! Fulfil all obligations ... and help you one another in righteousness and piety, ...". While the Prophet once said that:

"None of you is a true believer in Islam until and unless he loves for his fellow man what he loves for himself."

The above statements clearly reflect the extent of the relations between an individual and his fellow individuals in Islamic countries such as Saudi Arabia. This would mean that people in Islamic countries tend to identify their own interest with the interests of the society, indicating a greater acceptability of uniformity.

Hypothesis (7): "The larger the power distance in a society, the greater the acceptability of uniformity."

Power distance, from large to small, is defined as "the extent to which members of a society accept that power in institutions and organisations is distributed unequally" (Hofstede, 1987, p.4). In large power distance societies, there is a tendency for people to accept a

hierarchical order in which everybody has a place that needs no justification, while in small power distance societies, there is a tendency for people to ask for equality and demand justification for any existing power inequalities (Perera, 1989).

Hofstede (1987) has researched this subject over fifty countries, including Saudi Arabia. The result of his study put Saudi Arabia among the group of countries with large power distance. Accordingly, this suggests the acceptability of accounting uniformity in Saudi Arabia.

In addition, many government officials (Mr. Al-Amar, Mr. Al-Jarallah, Mr. Tawfeeg and Mr. Nasrallah of the Ministry of Finance and National Economy; Mr. Abdul Gafor, Mr. Al-Molhem and Mr. Jamjoom of the DZIT; Mr. Al-Hakmi of the Ministry of Planning; Mr. Al-Saad, Mr Muhana and Mr. Al-Ali of the National Accounts section, CSD; and Mr. Abu Hamed of the General Audit Bureau) have explained in interview the types of accounting problems they encounter, and when they were shown how a uniform accounting system might help in solving these problems, they positively welcomed the prospect. In the meantime, 17 out of 25 financial managers of the Saudi industrial corporations surveyed recommended the adoption of a set of rules or principles for classifying and recording accounting data to be applied by all business enterprises in Saudi Arabia (see chapter 6).

The idea of adopting uniform accounting system in Saudi Arabia was also supported by some accounting

professionals. For example, Mr Al-Rashed, managing director of a leading Saudi Accounting Firm, Al-Rashed Certified Public Accountants, though he dislikes the idea of uniformity for private sector companies, has emphasized the need for a uniform accounting system for government establishments such as universities and other public utilities (interview No. 11).

Thus, based on the above findings, it is concluded that Saudi Arabia provides a very favourable environment for a uniform accounting system. In connection with these findings, it is desirable to review the experience of other countries which operate uniform accounting systems, to contribute in better understanding and awareness of the main objectives and features of their systems. This is particularly important, because the idea of uniform accounting has been ignored so far in Saudi Arabia. Although France, which operates a comprehensive uniform accounting system, was among the countries selected for the purpose of developing accounting in Saudi Arabia, it was excluded at the comparative stage of the development programme. Perhaps this may be attributable to the fact that most members of the team involved in the project were American professionals and academics, and even the Saudi members among the team had received their higher education in the USA (see chapter 9).

10.4.7 Experience of Countries Operating Uniform Accounting System (UAS)

In the past, many countries, including centrally-planned economies, mixed economies and free-market economies, have chosen the uniform approach to develop their accounting system.

This section reviews the experience of two countries which have adopted a uniform accounting system, France and Egypt. This does not mean that the accounting system of these two countries is entirely suitable for the Saudi Arabia environment and thus should be adopted. However, France and Egypt were selected for closer study because they are representative of two different sets of environmental conditions. France is a developed free-market country which adopted uniform accounting to serve both micro and macro purposes for better national economic development planning. Most (1971, p.15) argued that:

"France presents us with a good example of the use of accounting for economic development ... We can only point to the fact that there has been, and still is, a widely held belief on the part of competent officials that accounting does have a significant part to play in the economic development of the modern state."

Egypt is a developing country with a centrally-planned economy which adopted uniform accounting for the purposes of macro planning as well as effective control by the state over its economic units, mainly public enterprises. Egypt was selected because of its long historical influence on both accounting education and

accounting practice in Saudi Arabia (see chapters 4 and 5). Thus, if Saudi Arabia is going to establish its own uniform accounting system in the future, undoubtedly Egyptian accounting experts would give great assistance in this respect.

10.4.7.1 France's Experience

10.4.7.1.1 General Background

The French have long recognized the desirability of standardisation in the presentation of financial information. This goes back to the Second World War, which had destroyed the French economy, thus, the first postwar French government was faced with the problem of stimulating economic recovery without delay. To restore and improve upon France's pre-war productivity, the country's productive structure needed to be rebuilt and modernized. This was the objective of the five-year economic plan which was prepared from scarce data, as there was no set of national accounts available (Fortin, 1991, p.4).

In order to enhance the national statistics and provide government with better accounting information, the Plan Comptable was formulated in 1947. It significantly revised in 1957 and again in 1982. These revisions were carried out in order to increase the appropriateness of the information content of final accounts and supplementary notes for users' needs, and, at the same time, to anticipate the requirements of the draft Fourth EEC Company Law Directive. Among the major

changes were a requirement that a company's financial statements must present a "true and fair view" of its financial position and results of operation, the combination of the trading account and profit and loss account into one statement, and the requirement that supplementary information and notes be mandatory (Oldham, 1987, p.65).

10.4.7.1.2 The Objectives of the French System

The French government believed that considerable advantages would accrue from standardised accounting, including better comparable information for shareholders, bankers and other third parties; and easier and quicker preparation of national statistics and accounts. More specifically, the French uniform accounting system was designed to achieve the following objectives (Oldham, 1987, p.145):

1. to promote more reliable national and fiscal policies;
2. to assist in eliminating fiscal inequalities;
3. to minimise social misunderstanding by informing the public of the true distribution of national wealth;
4. to provide data for the study of market trends;
5. to improve healthy competition;
6. to aid in the development of fairer taxation;
7. to provide shareholders, suppliers and bankers with an opportunity to exercise their judgement more satisfactorily;
8. to aid Government authorities in exercising controls;
9. to provide a clear and prompt view of financial results;

10. to permit analysis and comparison of manufacturing costs.

Enthoven (1973, p.226) pointed out that the French system "not only has proved extremely useful for social accounting and public administration (inc. taxation), but it has been also of great benefit: (a) for macro and micro planning; (b) to industries and industrial associations in making economic analyses and forecasts; (c) for structural analyses, and in measuring and comparing industrial productivity; (d) it furthermore tends to enhance the efficient administration of enterprises."

10.4.7.1.3 The Main Features of French System

The main feature of the French Plan Comptable is its applicability from the accounts-planning stage to the preparation of the annual accounts. The Plan Comptable prescribes the form and contents of financial statements. It incorporates a uniform chart of accounts which specifies the classification of items to be included in the financial statements. Furthermore, the Plan Comptable contains explanations of terminology, principles of measurement and valuation, and cost-accounting methods. The new French national chart includes nine main classes:

- Class 1 Capital
- Class 2 Fixed Assets
- Class 3 Inventories
- Class 4 Personal Accounts
- Class 5 Liquidity
- Class 6 Expenses
- Class 7 Revenue
- Class 8 Special
- Class 9 Cost Accounts.

The above accounts are codified on the basis of the decimal system, classification having been set up in accordance with economic and legal requirements. Classes 1-5 form the Balance Sheet Accounts; Classes 6-7 are the profit and loss accounts; class 8 is Special Accounts; and finally, class 9 Cost Accounts.

According to Nobes (1991, p.33) "The chart must be completed each year for national statistical purposes; tax returns are based on the plan; published financial statements use the model formats; and all the former use the standard definitions and measurement rules."

10.4.7.2 Egypt's Experience

10.4.7.2.1 General Background

Egypt is a developing country with a centrally-planned economy, and has operated a uniform accounting system since 1966. The importance of accounting uniformity was recognized after a series of nationalization decrees which were issued in 1956, 1961, and 1963 to eliminate the dominant role of both foreign and large-scale, local private capital.

In 1964, Law 129 established the Central Accounting Agency (CAA) as an independent institution reporting directly to the president. The CAA was created to supervise the functioning of the various accounting control boards by (a) auditing the final accounts of state enterprises; (b) reviewing the reports of external auditors of state enterprises; (c) comparing companies'

results with established plans; and (d) reporting violations of laws and regulations.

In 1966, a uniform accounting system was approved in Egypt, and has been applied from the financial year January 7, to June 30, 1968 (Briston and El-Ashker, 1984, p.131).

10.4.7.2.2 The Objectives of the Egyptian System

The Egyptian uniform system was issued to unify and control the flow of accounting data to its different users. More specifically, the system was designed to achieve the following objectives (CAA, 1966. pp.8-10):

1. provision of the necessary accounting information and analytical tools for planning, execution of plan, and control at all levels;
2. provision of links between micro-accounting on the one hand and macro-accounting on the other, thus contributing to the accuracy of national accounts based on business accounts of economic units;
3. facilitating collection, tabulation and storage of unified data.

Briston and El-Askhar (1984, p.145) argued, with reference to the Egyptian accounting system, that "various kinds of information at different degrees of detail can be easily collected at the state level within a comparatively short time." They also claimed that the system has proved successful in providing governmental bodies as well as management at the enterprise level with reliable financial information at the right time (Ibid).

10.4.7.2.3 The Main Features of the Egyptian System

The main features of the Egyptian uniform accounting system are (CAA, 1966, pp.15-16):

- A) The system is compulsory for all Egyptian public enterprises. Private enterprises can be required to apply the system by the relevant minister;
- B) The system is uniform which includes:
 - 1. chart of accounts;
 - 2. bases, rules, and definitions of accounting terminology;
 - 3. accounts and financial statements; and
 - 4. planning budgets.
- C) The system is flexible. This flexibility is reflected in the establishment of a permanent committee to provide a continuing review and appraisal of the system and to suggest revision if need arises.

One of the most important part of the Egyptian uniform system is the chart of accounts. This chart includes nine classes as follows:

- Class 1 Assets
- Class 2 Liabilities
- Class 3 Users of resources
- Class 4 Resources
- Class 5 Production Centres Control
- Class 6 Production Services Centres Control
- Class 7 Marketing Services Centres Control
- Class 8 Administrative and Financial Services Control
- Class 9 Capital Transaction Centres Control.

The above accounts are classified into three main categories, namely (1) balance sheet accounts, (2) operating accounts, (3) control accounts. The balance sheet accounts are divided into assets and liabilities; the operating accounts into uses and sources; and control accounts into production, production services, administrative and financing services, marketing services and capital expenditures. Each of these divisions is

identified by a one digit number (from 1-9), while the general accounts are identified by a two digit number.

Under the Egyptian uniform system, economic units are required to prepare the following statements and accounts (Briston and El-Askher, 1984, p.140):

1. Balance sheet;
2. Statement of changes in financial position;
3. Current operations account;
4. Production and trading account;
5. Profit and loss account; and
6. Cash flow statement.

In addition to the above statements and accounts, enterprise is required to prepare three different types of budgets: (a) production budget; (b) financial budget; and (c) cash budget. Each enterprise is also required to prepare monthly or quarterly statements, as well as the annual production and financial planning statements. Examples of such statements include statements of sources and use of products, goods for resale, production inputs, commodity inputs and production programmes.

To sum up, the brief review of the above two systems in current use shows that they are comprehensive and each designed to serve the needs of its own environment. The main purpose of the Egyptian system is to supply the National Planning Board with information to help control the operations of different enterprises under its control, while the aims of the French system are largely to ensure the provision of more relevant statistics and national comparability for economic, social and fiscal planning purposes. Evidence from the literature suggests

that they are successful to a certain degree, in meeting these objectives, each within its own environment.

However, it appears that the perspective of the Egyptian system is less safe than that of the French system, because the open-door policy in Egypt has increased the power of multi-national corporations and the big eight accounting firms as well as other international institutions such as the IMF.

As a result, there is a firm trend in Egypt nowadays to adopt IASs and encourage the accounting profession. For example, among the recommendations of national and international conferences on accounting and auditing held in Cairo (in 1980 and in 1986) were the preparation of accounting standards conforming with generally accepted international accounting standards and the production of auditing standards. This recent move in Egypt has been described as the major threat to its uniform accounting system (Briston and El-Askhar, 1984).

In addition, the Egyptian uniform system is linked with the political system (i.e socialism), and evidence shows that such systems are declining around the world, as shown by the situation in Eastern European countries and recently in the Soviet Union. This factor would undoubtedly increase the uncertainty surrounding the Egyptian accounting system.

In contrast, the French accounting system is based upon a free-market economic system such as has now spread all over the world. In the meantime, the French

plan has been adopted by some developing countries, particularly former French colonies. Moreover, the success of the OCAM plan, which closely follows the French plan, led to the establishment of a training and implementation package based upon the plan. The experience of Peru suggests that the plan can provide a quick improvement in the quality of national statistics (Briston, 1978, p.119).

Based on the above discussions and arguments it is perceived that it would be desirable for Saudi Arabia to concentrate on study and possible adoption of the French uniform system and to divert attention from the Egyptian and Anglo-Saxon accounting systems. It is worth mentioning here that the usefulness of the French plan has been recognised by several accounting scholars, particularly those who have experience of accounting information needs for economic development. Enthoven (1973, p.227), for example, argued:

"The French Plan Comptable may serve as a useful example for international economic coordination and integration, and for developing countries... The French experience seems to indicate that normalization of enterprise accounts can enhance the whole accounting methodology and practice, making accounting a more effective instrument in the economic process."

Parker (1985, p.81) claims that the French accounting system "is very useful in an economy which is centralised and closely regulated by the government."

Certainly the adoption of the French system should be considered only as a short term solution and eventually Saudi Arabia should establish its own national uniform system. In any case the question of whether to adopt the French system or to establish a new system remains a political one and may involve lengthy procedures and deliberations - a time which Saudi Arabia can ill-afford. The likelihood of long delay can be inferred from the length of time taken to establish some accounting and auditing guidelines: they took about six years to prepare and now, more than four years since they were first published, there is still much doubt as to their future. However, at this stage it is possible to propose a general framework by which accounting problems might be alleviated, and this is outlined in the next section.

10.5 Proposed Plan for Improving the Accounting System in Saudi Arabia

10.5.1 Background

Although methods of improving each accounting component have already been recommended in earlier chapters (see chapters 4 to 8), this section considers how the accounting system as a whole in Saudi Arabia could be improved. However, before answering such a fundamental question, it is worth summarizing the discussion so far in the following main points:

- 1) The accounting system and its components, or sub-systems (education, profession, enterprise, government

and national accounting) in Saudi Arabia suffer from various problems. The major problems which have been identified in each component are as follows:

- a. **Education Component:** A serious problem is the lack of textbooks based on local environment needs. Other problems include lack of qualified national accounting instructors. The emphasis is placed on external financial reporting, and private sector accounting. In contrast, less emphasis is placed on managerial and cost accounting, public sector accounting, computer accounting; and the current curriculum virtually excludes national accounting (see chapter 4).
- b. **Professional Component:** There is a shortage of national qualified accountants, and a lack of local training programmes, accounting rules and guidelines for accounting practice. Cooperation among professionals on the one hand, and between the professionals and the Ministry of Commerce on the other, is inadequate. There is no professional accounting body and no formal code of ethics (see chapter 5).
- c. **Enterprise Component:** There is a shortage of qualified personnel. Forms, procedures, and records are deficient. There is a lack of linkage between the enterprise accounting system and the national accounting system. Internal audit is weak. Accounting reports are diverse and inconsistent.

There is little appreciation of the use of accounting techniques for planning and control purposes (see chapter 6).

- d. **Government Component:** There is a lack of qualified personnel. The government accounting rules and the system of classification of accounts are inadequate, because they were designed long ago and have not been amended adequately to reflect the rapid changing in the public sector. The state budget is still a traditional budget, with more emphasis upon the input side. Audit in the public sector places more emphasis upon financial and compliance audit, with very few attempts to carry out value for money audit. There are delays in the preparation of the state final accounts. The controller and the manager in most government-owned enterprises belong to the same organisation (see chapter 7).
- e. **National component:** Most of the problems of the national component occur as a result of the deficiencies of the above four components, because they play a significant role in the input data required for the construction of this component. For example, the lack of qualified accountants, absence of linkages between micro accounting and macro accounting, delay in the State final accounts, and the poor quality of the classifications used in statistical abstracts, all

affect the construction of national accounts and consequently reduce the reliability of the output data which are mainly used for planning and control at the national level (see chapter 8).

- 2) The study has revealed that, so far, very little has been done to alleviate these problems. Although the government in recent years has recognised the problems in the professional component, and attempted to establish some accounting and auditing guidelines, most of the efforts have been carried out by foreign accounting experts as well as Saudi academics, with very little participation by local professional accountants. Meanwhile, review of the contents of the guidelines published so far shows that they are based upon American and British accounting theories, principles and practices, with the main emphasis being upon the needs of external users, mainly shareholders and creditors. The needs of government agencies responsible for planning and controlling the national economy, together with public sector lending agencies, are entirely excluded (see chapter 9).
- 3) It has been argued in this chapter that the adoption of a uniform accounting system along the lines of the French system would alleviate most of the above accounting problems and consequently improve accounting information. It was also found that the prevailing conditions and circumstances of the accounting environment in Saudi Arabia indicate that a

national uniform accounting system would be both desirable and feasible.

10.5.2 An Accounting Development Plan

The preceding section suggests that the accounting system and its components in Saudi Arabia suffer from various problems and that so far, very little has been done towards solving them.

A suggested solution is now proposed: a comprehensive accounting development plan (referred to as "the plan" from now on in this section). The plan is based upon the socio-economic development needs of Saudi Arabia, which urgently require simultaneous improvement of all components the accounting system (education, profession, enterprise, government and national). More specifically, the significance of the plan lies in its ability to achieve the following objectives:

1. incorporate all accounting system components into a single framework (see figure 10.4) which would undoubtedly lead to better understanding of their main problems, particularly as some of these problems overlap, that is to say the problems of one component affect another component.
2. identify and eliminate, or at least reduce the major shortcomings inherent in the present accounting system as a whole;
3. enhance the flow of accounting information from various economic sectors to the ultimate users; and

4. lead to an efficient allocation of scarce resources through the provision of balanced accounting information, which would enhance economic decision-making at micro and macro levels, in both the public and private sectors.

10.5.3 The Approach of the Plan

The plan is based on the System Approach to the problems. The questions now arise, what is the system approach; and is it possible to apply such an approach to accounting problems? Wilkinson (1986, p.32) states that the system approach "encourages a holistic viewpoint - that is any system (or problem) is best viewed as a whole having interrelated parts. ... the term implies that a systematic (i.e., carefully planned, step-by-step) development procedure leads to the soundest result."

As for the application of the system approach to accounting problems, it was shown that accounting in developing countries should be viewed as a system consisting of five components (sub-systems): the teaching of accountancy in educational institutions, the local accounting profession, the accounting function in indigenous enterprises, the accounting function of government agencies, and the accounting function at the macro level. The accounting establishment is viewed as a system and its constituent components are interrelated such that the behaviour (including problems) of one component affects the behaviour of the others. The

accounting problems in each component have already been identified and discussed earlier (see chapters 4-8).

10.5.4 The Process of Executing the Plan

At the outset, the plan assumes the willingness of accounting academicians, public accountants, and government officials, particularly those involved in planning, implementation, and control of the economic and financial activities of the country, to participate in the accounting improvement process. The key steps of the plan include the following:

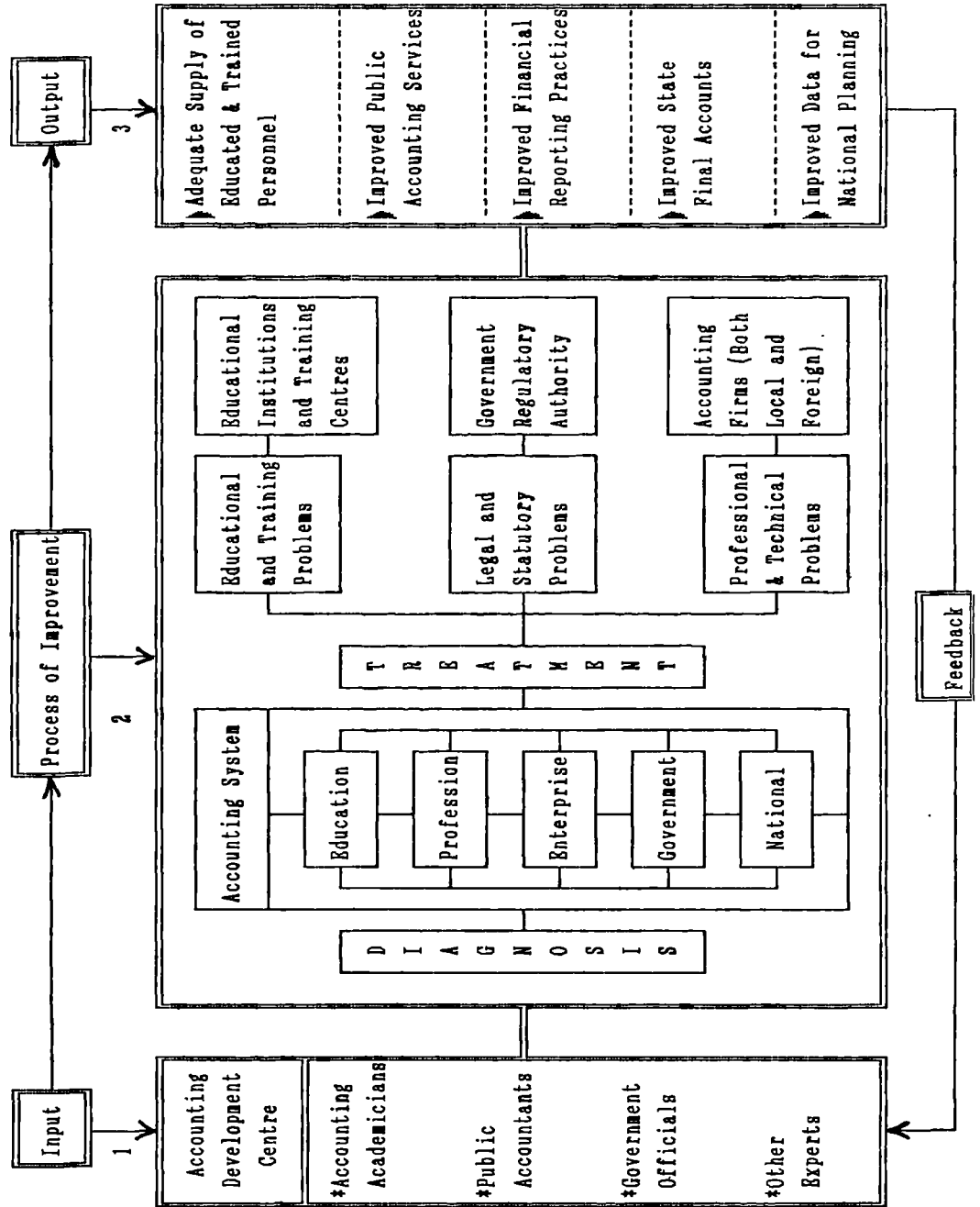
The first step (block 1 of figure 10.4) of the plan calls for the creation of an accounting body to be called the "Accounting Development Centre" in which the above three groups are represented. More specifically, the main task of the proposed ADC would be to direct all efforts toward the achievement of the following objectives:

1. develop effective educational accounting programmes which suit local environment needs;
2. develop accounting principles, formats and procedures that are relevant to local environment needs;
3. organise regular training programmes for local accountants to improve rendered services.

The second step (block 2 of figure 10.4) of the plan represents the actual accounting improvement process. This can be carried out in two main stages as follows:

1. **Diagnosis:** At this stage, representatives of each of the three groups (accounting academicians, public accountants and government officials) should study and

Figure 10.4: Plan For Improving the Accounting System in Saudi Arabia



analyse their respective components. Other experts may also be invited to give their assistance at this stage. The aim of the diagnosis process is to identify the accounting problems in each component. Although most of these problems have already been identified and discussed by the present study, others may need further study and research. In any case, these problems can then be arranged according to their urgency for treatment.

2. **Treatment:** The aim of this stage is to prescribe the action to be undertaken in order to solve the problems identified in the previous stage. For better and systematic treatment, it is appropriate to classify these problems into three main categories as follows: educational and training problems, legal and statutory problems, and professional and technical problems. Having done so, the treatment can be carried out through three main channels: educational institutions and training centres, government regulatory authorities, and accounting firms (both local and foreign). The role of each of these groups in the process of accounting problems treatment is explained below.

a. **Educational Institutions and Training Centres:** At the outset, the educational institutions currently offering accounting courses both below and at university level should recognize the importance of sound accounting education in the socio-economic

development planning process in Saudi Arabia. A clear analysis and evaluation should be made of the availability and the actual needs of accounting manpower. In this connection, it might be desirable to have an accounting manpower inventory and accounting development plan prepared, which would set forth the needs for various areas of accounting and auditing under the current and future five-year development plans. Moreover, due to the great shortage of national educators and trainers, the proposed "Accounting Development Centre" and the types of updating to be entered into, could be subject to refinement in view of the needs of the various sectors of the economy. In this regard, the areas of concentration and text materials may have to be spelled out; for example, there could be a considerable need for more training in electronic data processing (EDP), etc. Here the training centres which currently operate throughout the Kingdom under the authority of GOTEVT could play a significant role in training local accountants, not only in EDP, but also in other aspects such as bookkeeping and clerical work.

- b. **Government Regulatory Authority:** Since there is no accounting professional body in Saudi Arabia, accounting systems and practices operate entirely under the Government authority, represented by the Ministry of Commerce. Currently, the Ministry of

Commerce monitors the accounting systems and practices through two main legislations, namely: the Companies Act of 1965 and the Accountants Law of 1974. However, these two acts suffer from serious shortcomings and need urgent amendment to reflect the current environment needs.

1. The Companies Act should be amended to incorporate measurement, classification, valuation and reporting criteria for keeping accounts based on a relevant set of concepts, standards and rules. Furthermore, it must be geared soundly to the national accounts and to the requirements of other economic analysis and policies.

2. The Accountants Law of 1974: This Law merely prescribes the conditions and outlines the rules to be followed after licensing. It virtually excludes accounting standards, ethical standards or a code of professional conduct. Thus, there is an urgent need to amend this Law to include the above issues and to incorporate the recent accounting and auditing guidelines.

c. **Accounting Firms:** Accounting firms (both local and foreign) operating in Saudi Arabia could play a significant role in the accounting improvement plan. For example, they could use their expertise to assist in the various phases of accounting development, particularly the project appraisal cycle, capital markets and taxation. They should

also, as far as possible, engage and train local staff and give them a fair chance to advance. This is very important to enable personnel, especially new accounting graduates, to gain practical experience.

10.5.5 The Expected Outcomes of the Plan

The plan (block 3 of figure 10.4) shows five desirable outcomes of the coordinated development of all accounting system components, as follows:

1. improvement in accounting education and training, to provide an adequate supply of educated and trained accountants who could contribute positively to the socio-economic development planning of the country;
2. improvement in the quality of public accounting services;
3. improvement in the financial reporting practices which would increase users' reliance on and use of financial reports in their investment decisions;
4. improvement in the accounting system of government agencies and speeding of the preparation and submission of the state final accounts, which currently suffer from long delay;
5. as a consequence of the above factors, improvement in national accounting data to be used by government for socio-economic development planning.

The suggested plan is comprehensive, systematic and locally feasible. However, for the success of the plan, effective cooperation should be established between the

three participant groups. Strong support from both government and the business community is also needed in terms of finance and actual participation in the plan activities.

10.6 Summary and Conclusion

The first part of this chapter focused upon development planning in Saudi Arabia and its needs. Issues discussed included, among other things, reasons for planning, the planning system, the process of planning, accounting information needs for the formulation and implementation of national plans, development projects and Specialized Credit Institutions.

It was shown that since 1970 Saudi Arabia has adopted a comprehensive development planning approach. Economic planning was deemed necessary by the Saudi government due to the primitive state of the economy infrastructure and the inability of the domestic private sector to take on the development task. That inability is mainly due to the small size of private sector and the nationwide shortages of human and financial capital (Al-Jasser, 1986). Development planning in Saudi Arabia is mandatory for all public sector units, while it serves as a guide for private sector units. Although all government agencies are involved in the planning process, the key role is assigned to the Ministry of Planning.

It was also shown that one of the main problems facing the planners in Saudi Arabia is the lack of accounting information, both in terms of quantity and

quality. This was confirmed recently by the writers of the Fifth Development Plan (1990-95, p.75) and by the Deputy Assistant to the Minister of Planning, during the course of interview by the author (interview No. 7).

The second part of the chapter discussed the uniform accounting approach as an alternative to accounting diversity, and showed how, if adopted, uniformity could facilitate information provision for socio-economic development purposes in Saudi Arabia. It was suggested that most of accounting shortcomings in Saudi Arabia would be alleviated by the adoption of a uniform accounting system, as such a system would facilitate the collection and storage and communication of accounting information, and facilitate the training process and transfer of "know how" skills. It was also found that the prevailing conditions and circumstances of the accounting environment in Saudi Arabia indicate that a national uniform accounting system would be both desirable and feasible. These conditions and circumstances include, among other things, centralised development plans, the need for economic development, the small size of the private sector, the relatively low education level, the weakness of the accounting profession, the low level of management training, and the large power distance.

However, such a system will take a long time to establish. Thus, a comprehensive accounting development plan was suggested. This plan is based on the socio-economic development planning needs of Saudi Arabia,

economic development planning needs of Saudi Arabia, which urgently require simultaneously a need for improvement of all accounting system components (education, profession, enterprise, government and national accounting) by integrating them into a single framework of action, as shown in figure 10.4 above. The suggested plan is comprehensive, systematic and locally feasible. However, the success of the plan, or any other strategy for improving accounting systems and practices, would be partly dependent upon the support of the government, as well as the business community in Saudi Arabia.

CHAPTER 11

SUMMARY, CONCLUSIONS, AND RECOMMENDATIONS

11.1 Introduction

This chapter summarizes the findings and conclusions presented in the foregoing chapters. The purpose is to bring together and underline the main ideas related to the theme of the study.

As the title suggests, this chapter includes three main sections. The first section provides a brief discussion of the objectives of the study, and the study methodology used to accomplish those objectives. Section two delineates conclusions reached based upon the theoretical analysis and empirical surveys. The final section provides recommendations for improving accounting in Saudi Arabia.

11.2 Summary

The need to study the evolution of accounting in its environmental setting in developing countries is increasingly recognised in the literature (Jaggi, 1973; Enthoven, 1973 and 1977; Radebaugh, 1975; Briston, 1978; Wallace, 1990). The purpose of this thesis is to examine the evolution and status of accounting systems in developing countries, with particular reference to the Saudi Arabian environment. It attempts to highlight the main shortcomings in each component of the accounting system (education, profession, enterprise, government and national accounting) and to put forward suggestions and

recommendations for improvement which reflect the socio-economic development needs.

The study was carried out because there is a notable lack of comprehensive accounting research in developing countries in general and in Saudi Arabia in particular. In Saudi Arabia, for example, efforts so far, including the recent accounting developments supported by the Ministry of Commerce, have concentrated upon the accounting profession and external financial reporting. It should be pointed out, however, that the present unsatisfactory state of affairs cannot be blamed on these two accounting issues alone; it is the end product of a complicated causal system. Therefore, any programme of action aimed at making accounting a more useful tool in the economic development of Saudi Arabia must be based on thorough consideration of the problem as a whole, with all its components (education, profession, enterprise, government and national accounting). With this in mind, the present study was basically designed to accomplish the following objectives:

1. To determine the current status of the accounting education and the accounting profession, and the environmental factors affecting these two components (chapter 4-5).
2. To examine the prevailing accounting recording, classification and reporting procedures at both micro (enterprise and government) and macro (national) levels in Saudi Arabia, in order to find out whether

they provide information relevance to the socio-economic environment (chapters 6-8).

3. To review and evaluate the new accounting and auditing guidelines which were introduced recently in Saudi Arabia (chapter 9).
4. To discuss the accounting information that is actually needed in Saudi Arabia, particularly for the construction and implementation of national development plans, and to show how such information could be best reported to the ultimate users. For example, would uniform accounting approach be of greater advantage than flexible approach in this respect? (chapter 10).
5. To draw the attention of the authorities and accountants in Saudi Arabia to the shortcomings of various accounting aspects, and to convince them that the best approach is to tackle such shortcomings simultaneously (chapter 10).

In order to accomplish the above objectives, the study began with a brief review of the function of accounting in economic development, the common accounting problems in developing countries, and the main approaches suggested for improving accounting in these countries (chapter 2). This review was considered necessary for several reasons: First, most developing countries, including Saudi Arabia, have adopted a comprehensive development planning approach as the principal means towards the achievement of accelerated growth. Therefore,

for any accounting study in these countries, it is important to highlight the function of accounting in this vital area. Second, most developing countries have common accounting problems, and reviewing these problems will undoubtedly increase our understanding of accounting problems in Saudi Arabia. Finally, Saudi Arabia is now in the process of developing its own accounting system. Therefore, it is important at this stage to be aware of the approaches suggested for improving accounting in developing countries in general, particularly as such approaches have not been considered by any previous accounting studies in Saudi Arabia. Instead, the attention so far seem to have focused upon the British and American accounting approaches as a path for developing accounting in the Kingdom. This part of the study was carried out by means of library research in the United Kingdom. Several studies, articles, and reports were reviewed. Some of these materials were obtained through inter-library loans services.

It was also necessary to examine the environmental characteristics (social, political, regulatory and economic) in which accounting operates in Saudi Arabia (chapter 3). Thus, several documents and copies of decrees, laws and regulations related to the economic and business environment were obtained from official sources in Saudi Arabia. All these documents were in Arabic and had to be translated into English by the author. Some materials related to the Saudi environment were found in

the Arab Gulf Studies Centre, University of Exeter, England. Two visits were arranged by the author for this purpose.

As there are few published materials concerning the accounting systems, practices, classification, policies and reporting procedures, the author arranged for a field trip to Saudi Arabia, which lasted for three months, and collected the necessary data by using a combination of two sets of questionnaires and interviews. The first questionnaire (see Appendix A) was addressed to sample of 100 public accountants, of which 86 replied. This questionnaire was designed to reveal some vital aspects of current accounting practices in Saudi Arabia. Matters investigated included the type of accounting standards widely referred to by accountants, reasons behind the spread of foreign accounting standards in Saudi Arabia, the relevance of such standards to the Saudi socio-economic environment, and types of accounting services rendered. It also aimed to seek public accountants' opinions regarding the recent accounting developments in Saudi Arabia, e.g. the extent to which local accountants were actually involved in the establishment of the accounting and auditing guidelines produced so far, why these guidelines have not become mandatory, so long after their publication, and the future of these guidelines. Responses received concerning these issues were analysed and discussed in chapter 5.

The second questionnaire (see Appendix B) was addressed to the financial managers of 25 Saudi corporations operating in the industrial sector, which form 37% of the existing corporations as at the end of 1989. This sector was selected because it has always been given high priority in overall development plans and has a potential role to play in the economic diversification. The survey here concentrated on the main features of the accounting systems of these enterprises (e.g. the design of the accounting system, data processing method, chart of accounts, financial reports currently prepared, their frequency and their users); rules, procedures and principles in practice; the extent of use of accounting techniques for planning and control purposes; relationship to national accounts; accounting manpower problems and other related issues. Responses received concerning these issues were analysed and discussed in chapter 6.

Interviews were conducted with government officials in the Ministry of Finance and National Economy, General Audit Bureau, National Accounts Department, and Ministry of Planning (see Appendix C for a List of Names). The aim of these interviews was to gather data concerning accounting systems, classifications and reporting procedures used in the public sector (chapters 7-8).

Data collected from the theoretical study and from the empirical work were summarized, formulated and presented in narrative and tabular form as appropriate.

Analysis focused upon the environmental characteristics (social, political, regulatory and economic) in which accounting operates in Saudi Arabia, the status of the accounting system and practice, the recent accounting approach, the socio-economic development needs, and how the overall accounting system could be improved to satisfy these needs more fully.

The thesis is broadly divided into three related parts: the first part (chapters 1-3) is intended to provide a general background to the study, in which the objectives, significance and methodology of the study were set out; the role of accounting in economic development planning, the common problems of the accounting in developing countries, and the main approaches suggested for improving accounting in these countries were highlighted; and the environmental characteristics (social, political, regulatory and economy) in which accounting operates in Saudi Arabia were analysed and discussed.

The second part (chapters 4-8) was devoted to the current status of the accounting system in Saudi Arabia. This part presents a more or less a comprehensive analysis and evaluation of accounting education, the accounting profession, enterprise accounting, government accounting and national accounting in Saudi Arabia.

The third part (chapters 9-10) dealt with the recent accounting standardisation programme and the contents of accounting and auditing guidelines established so far. It

also discussed the socio-economic development needs of Saudi Arabia, and proposed a plan which urgently requires simultaneous improvement of all components of the accounting system (education, profession, enterprise, government and national).

11.3 Conclusions

Based on the review of related literature, data collected from Saudi Arabia, and the researcher's own observations, several major conclusions are reached. These conclusions are summarized below under five main headings: (1) general conclusions; (2) accounting environment in Saudi Arabia; (3) the status of the accounting system; (4) the recent accounting approach; and (5) the socio-economic development needs of Saudi Arabia.

11.3.1 General Conclusions

Based on the review of related literature, the following general conclusions can be drawn:

1. Developing countries differ widely with respect to the stage of economic and social development, natural and human resources, and attitudes and values.

2. Most developing countries have adopted the economic development planning approach as the principal means towards the achievement of accelerated growth.

3. Accounting plays an important role in economic development planning and such role is likely to continue. This role arises from the need for quantitative and

financial data and accounting techniques for the preparation, implementation and control of national economic plans.

4. In many developing countries social, economic, and political problems are the main concern of the people and authorities; as yet, accounting does not occupy a position of importance.

5. Accounting in developing countries suffers from various shortcomings, the scale of which varies from one country to another. In view of these shortcomings, various approaches have been suggested for improvement. Although these approaches have a common objective (i.e. to improve accounting in developing countries), they vary in terms of their conceptual framework and in their view of the way that accounting problems in developing countries should be tackled (see chapter 2).

11.3.2 Accounting Environment in Saudi Arabia

Accounting is largely a product of its environment and is also a vital force which is able to shape that environment. The study has shown (see chapter 3) that Saudi Arabia is an Islamic State in which religion plays an important role in the social, political, legal and economic environment of the Kingdom. It has also shown that unlike most developing countries, Saudi Arabia has never been a colony or subject to foreign rule. Its political system is based on the Holy Qura'n and traditional Sharia (Islamic Law) and all decisions of the government are guided by them. In spite of all the

changes and developments in Saudi Arabia, Islam has remained at the centre of all the activities and has been the ultimate guiding force.

The Government of Saudi Arabia, by means of the Council of Ministers' Resolutions and Royal Decrees, has enacted a numbers of laws which include Companies Law, Income Tax Law, Certified Accountants Law and Foreign Investment Law. Some of these laws have been amended, or replaced, to provide regulations better suited to the needs of the country. However, others still need further study and revision. The positive aspect of these laws is that they include some accounting and auditing guidelines, particularly with regard to the company's accounts, appointment of the auditor; his independence, rights, duties, and responsibilities. However, nothing have been stated about the format, layout, procedures and contents of financial reports in any of these laws.

As for the economic environment, it was shown that although Saudi Arabia was founded as a Kingdom in 1932, much of its economic development took place comparatively recently. It was only in the 1970s that efforts were made to develop the economy, and create a national infrastructure of modern highways, ports, airports, schools, and hospitals. With the oil price rises in 1973-74, the resources to finance development increased enormously, and there was a rush to create a modern infrastructure as quickly as possible. The speed of implementation resulted in some waste, but overall the

first, second and third development plans were successfully implemented, and the structure for a modern unified economy created. However, in recent years the pace of development has slowed, partly reflecting oil production cut-backs and price falls, with a marked deterioration in terms of trade. At the same time, less investment has been needed, with the completion of major infrastructure projects.

11.3.3 The Status of the Accounting System

11.3.3.1 Accounting Education

The study has shown (see chapter 4) that accounting education in Saudi Arabia basically operates within the framework of the education system of the country as a whole. This education system has two distinct characteristics: it is traditional, emphasising Islamic teachings and principles and stressing the role of Saudi Arabia as the preserver and protector of Islam; and it focuses on Western institutions, methods and technological innovations as a means of improving Saudi Arabian society.

Accounting education in Saudi Arabia consists of two main levels, below university and university level. The former includes the secondary commercial schools and the Higher Institutes for Commercial and Financial Science, while the latter includes university colleges which provide undergraduate and postgraduate programmes in accounting.

Despite some problem areas within the current accounting education system (e.g. shortage of local instructors, textbooks and lack of research), the present university undergraduate accounting programme leading to the B.A. degree, and the graduate programme leading to the M.Sc. degree, seem to be adequate, compared with similar programmes in other developing countries. Moreover, many graduates of these programmes have been admitted to postgraduate accounting programmes in developed countries such as USA and UK.

11.3.3.2 Accounting Profession

The study has shown (see chapter 5) that the accounting profession in Saudi Arabia is still in its infancy. For all practical purposes, 1974 may be considered as the date of its real origin. The accounting profession has not developed sufficiently to keep pace with the rapid economic development which has occurred during the last two decades. Its future development hinges very much on an effective professional body, setting qualifications and carrying out enhancement activities.

The major deficiencies of the accounting profession are the absence of a professional body, local accounting principles, code of ethics, and institutional support. The Higher Committee of Certified Accountants, which now monitors the accounting profession, is unable to fulfil its role toward the development of this component,

because its members are part-time staff and too busy to do so.

In addition, the empirical survey, which was designed to examine some practical aspects of current accounting practices in Saudi Arabia, revealed the following:

1. Public accountants in Saudi Arabia have a variety of experience, which contributes to the diversity in accounting practices.

2. There are various accounting standards found in Saudi Arabia, mainly the USA and the UK standards, and IASs. However, the IASs are widely used in practice.

3. The absence of national uniform accounting standards is believed to be the main reason for the spread of foreign accounting standards in Saudi Arabia.

4. The language and content of auditors' reports differ greatly from one accounting firm to another.

5. Auditing, and income tax and Zakat are the two most important services provided by the accounting firms in Saudi Arabia. Management advisory services presumably are not in great demand at the present time.

6. Very few local professional accountants participated in the establishment of the recent accounting and auditing guidelines.

7. The problems of enforcement and institutional support, together with lack of cooperation from the interested parties, are believed to be the main reasons

for failure to implement fully the accounting and auditing guidelines established so far.

11.3.3.3 Enterprise Accounting

In recent years, a number of business enterprises have been established in Saudi Arabia as a result of the rapid development in almost every economic sector. These enterprises take various forms, ranging from General Partnership (private company) to Corporation (public company). The latter is the largest type of business enterprise found in Saudi Arabia in terms of capital (see chapter 6).

An analytical study based upon a survey questionnaire submitted to 25 Saudi public corporations operating in the industrial sector, as well as a review of their published financial reports, revealed the following:

1. There are considerable differences in their accounting systems and reporting procedures, which affect accounting information, in respect of both quantity and quality.

2. The main reason for these differences is the absence of local requirements, since neither the Companies Law nor the Income Tax and Zakat Regulations specify any particular accounting guidelines to be followed.

3. Although all enterprises included in the survey comply with statutory requirements concerning the preparation of a balance sheet, profit and loss account,

and directors' reports, other reports such as statement of source and application of funds and changes in financial position are not commonly prepared, despite their importance.

4. It was also found that the enterprises in question gave comparative figures for only two periods, the present and the preceding year. However, this is not very sound from a time-series analysis point of view, because such a short period may not reveal trends or may have been distorted by individual events.

5. The use of accounting techniques for the purposes of planning and control is limited. This was attributed to the weakness of the internal control system and the cost accounting system, as well as the shortage of accounting manpower.

6. The current accounting systems of these enterprises provide very little information relevant to the construction of national accounts. This was attributed to the absence of statutory requirements, the nature of the current accounting systems of these enterprises, and the lack of awareness of the national accounts' needs.

7. Very few enterprises disclose non-financial information such as employees' welfare, donations for social causes, encouragement of use of Saudi employees, health and safety protection, and pollution control. Although these enterprises, when advertising for new accounting personal, state that "priority is given to

Saudi nationals", they impose very high conditions which would be unlikely to be met by new Saudi accounting graduates.

11.3.3.4 Government Accounting

The study has shown (see chapter 7) that the government accounting system is out of date, taking into account the size of the government sectors and the complexity of government transactions today, compared with when the system was first established in 1956. The current government accounting systems, procedures, format and classifications are lengthy and complex. For example, payment vouchers have to go through various departments, be checked, and rechecked, and the signatures of various officials have to be obtained before the amount is finally paid. These long procedures and their excessive rigidity have undoubtedly hampered the development of the accounting system.

Furthermore, the state budget has to go through many phases before it is finally approved and executed. The budget is still a traditional or "line-item" budget, which includes certain economic functional classifications, without further useful breakdown and evaluation into programmes, activities and projects. This type of budgeting is simply a system for allocating particular kinds of inputs, which are not related in any way to the intended outputs, let alone the outcomes. Nor does it enable auditors to conduct any other audit, apart from financial and compliance audit.

As far as accountability is concerned, there are serious deficiencies. For example, the role of both the FRA and the GAB is limited to pre- and post-control voucher audits of governmental transactions respectively. Such audits are basically concerned with the legality of transactions, to determine whether transactions are properly conducted, in accordance with applicable laws and regulations. Although this kind of audit provides some relevant information for the purpose of accountability and stewardship, it provides very little information relevant to the optimal use, control or performance evaluation of scarce resources and their management. No attention is given, however, to any type of economic audit or value for money audit.

11.3.3.5 National Accounting

National accounting is a vital economic instrument for execution of the economic plan by collecting and consolidating information on the implementation of the plan by different sectors, and comparing it with the target. The study has shown (see chapter 8) that the national accounts in Saudi Arabia are based on the UN system of 1968. However, due to the lack of statistical data and other problems, the UN system is not comprehensively implemented. As a result, the national accounts currently prepared by the CDS do not include input-output tables, a flow of fund statement, and a national balance sheet. The main reason for the absence

of these tables, according to national accounts officials, is the absence of data on which to base them.

The study has also shown that currently there are no statutes or professional accounting regulations that require companies to prepare and publish financial information for national accounts purposes. Indeed, even the recently stated objectives of financial statements in Saudi Arabia exclude the accounting information needed by government for the purpose of national accounts, merely saying that the government has the ability to obtain the information that it needs. However, nothing is mentioned about how and when such information can be obtained. Much, therefore, needs to be done to improve national accounts in Saudi Arabia. Perhaps the most urgent need is to have a more uniform system of accounts and better definitions of accounting data. Such improvements must be seen in the context of overall accountancy development and should be reflected in all components of the accounting system (education, profession, enterprise, government and national accounting).

11.3.4 The Recent Accounting Approach

In recent years, a number of developing countries have rushed either to adopt International Accounting Standards (IASs) or to develop accounting standards similar to those of the UK and the USA. This latter phenomenon became apparent in Saudi Arabia when the Ministry of Commerce agreed to finance a project which

aims to set accounting and auditing standards for financial reporting. The project was carried out by a team of accounting experts from the UK and the USA as well as Saudi Arabia.

It appears from the Analytical Study attached to the statements published so far that the working team has considered two types of accounting systems. The first is a flexible accounting system, i.e. an accounting system which allows a wide of choice among different accounting methods and procedures for the same transaction, as found in the UK and the US. The second is a uniform accounting system, in which accounting methods and procedures are established on a uniform basis, as in France and Tunisia.

Although both systems were considered in the comparative stage of the accounting development programme, preliminary findings published so far suggest that the first system, i.e. a flexible accounting approach, biased toward the American and British style, has been chosen as the path for developing accounting in Saudi Arabia.

There is no doubt that a move has taken place for the first time toward the advancement of accounting in Saudi Arabia. However, review and analysis of what has been published so far (see chapter 9) revealed the following:

1. The efforts so far have been confined to setting accounting and auditing standards for external financial reporting, resembling those of the UK and the USA, with

more emphasis upon the information needs of investors and creditors.

2. It is argued that the UK and USA accounting systems are mainly designed to satisfy the stock market and its users, and this study has shown that in Saudi Arabia there is no formal stock market, and the current number of listed corporations is very small compared to that in the UK and the USA.

3. It is also argued that the procedures for setting accounting standards for external financial reporting are very complex and can only be operated by a sophisticated body of accountants, which is hardly to be found in Saudi Arabia, at least for the time being.

4. At best, external financial reports represent only a small part of the overall objectives of accounting, while in Saudi Arabia, there is evidence that such reports are neither read nor understood.

5. A large proportion of the existing industry in Saudi Arabia, including all public utilities and major industries such as oil and petrochemical industries, is managed and controlled by the government which needs information different from that produced by the external financial reports.

To sum up, in Saudi Arabia, as a developing country, it seems that standards for external financial reporting set along Anglo-Saxon lines present considerable difficulty and might not satisfy the current socio-economic development needs of the country. More

specifically, Saudi Arabia needs an accounting system which provides information relevant to its socio-economic development planning, rather than one which is designed to furnish information to the stock market and its decreasing and uninterested body of shareholders.

In contrast, the present study suggests that most accounting shortcomings in Saudi Arabia would be alleviated by the adoption of a uniform accounting system, as such a system would facilitate the collection, storage and communication of accounting data, and facilitate the training process and transfer of "know-how" and skills. It was also found that the prevailing conditions and circumstances of the accounting environment in Saudi Arabia indicate that a national uniform accounting system would be both desirable and feasible. These conditions and circumstances include, among other things, centralised development plans, the need for economic development, the small size of the private sector, the relatively low education level, the weakness of the accounting profession, the low level of management training, and the large power distance.

In the meantime, review of the experience of countries operating uniform accounting systems suggests that such systems are successful to a certain degree, in meeting their objectives, each within its own environment. These environments, for example, include a developed free-market, France, and a developing centrally-planned economy, Egypt, (see chapter 10).

11.3.5 Socio-Economic Development Needs

"Accounting has to be in tune with the economic framework in which it operates and with the socio-economic requirements of society" (Enthoven, 1991, p.257). This study has shown (see chapter 3) that Saudi Arabia is a developing country which has adopted a comprehensive development planning approach as its vehicle towards growth and socio-economic development. Economic planning was deemed necessary by the Saudi government due to the primitive state of the economy's infrastructure and the inability of the domestic private sector to take on the development task. That inability was mainly due to the small size of the private sector and the nationwide shortage of human and financial resources (Al-Jasser, 1986). Development planning in Saudi Arabia is mandatory for all public sector units, while it serves as a guide for private sector units. Although all government agencies are involved in the planning process, the key role is assigned to the Ministry of Planning.

Accurate and timely information reflecting real economic conditions is essential for an effective planning process and for the effective economic development needed by any developing country such as Saudi Arabia. The value of accounting for economic development depends upon its ability to generate useful standardised economic data for planning, decision-making and control of economic activities at both micro and macro levels. For example, at the micro level, planners

need accounting information related to purchases of produced inputs, purchases of imports, value added, depreciation, sales of intermediate products, final sales and inventory investments, while at macro level, planners need accounting information related to the level of saving, investment, and consumption. Extensive and coherent information about the regional distribution of government services and economic activities are also needed to achieve balanced development in Saudi Arabia.

However, evidence shows that information such as those noted above are not available on time, in proper formats and of sufficient accuracy (see chapter 10). This is because in Saudi Arabia, micro accounting, including the recent developments, is based on the Anglo-Saxon accounting system, which virtually excludes the needs of the government or the public sector (Briston, 1978), while macro accounting is based on the UN system, which is difficult to implement in a comprehensive manner at the present time, due to the absence of basic input data as well as the conceptual difficulties associated with the system itself (see chapter 8).

Thus, it has become apparent that a number of improvements need to be made so that accounting may assume an effective role in the economic development process of Saudi Arabia. Recommendations as to the measures necessary for the improvement of the accounting system are presented in the following section.

11.4 Recommendations

Based on the research findings and conclusions, a number of recommendations may be made to improve the accounting system in Saudi Arabia.

11.4.1 Accounting Education

Accounting education should be more responsive to the country's present and future needs. In order to achieve this objective, the following are recommended:

1. More emphasis should be given to such areas as performance and programme budgeting, managerial techniques and insight into national accounting. Such courses should be incorporated into the present programme.

2. Textbooks and teaching materials tailored to the Saudi Arabia socio-economic environment needs should be improved and developed. Case studies of Saudi Arabian business enterprises must be collected and developed.

3. Better teaching techniques, such as visual aids and computing facilities should be used more frequently.

4. Practice sets should be included as a part of the accounting curriculum to inject real-life situations into the class-room. For example, the teaching of accounting at the universities could benefit by the "case methods" approach, while closer contacts with enterprises and governmental departments also could give students some sound practical experience.

5. More cooperation is required among Saudi universities, particularly in the areas of curriculum

design, and writing of books and other teaching materials which reflect socioeconomic environment needs.

6. More emphasis should be placed upon the accounting information needs of the public sector rather than concentrating solely on the needs of the private sector.

7. There is a need to teach basic accounting courses at the general secondary school level, so that students may gain experience of accounting early enough to consider it as a career. This is particularly important, because under the current accounting education system, most students learn about accounting only when they reach university. Although accounting courses are taught in the commercial secondary schools, there is very little opportunity for graduates from these schools to attend university, due to the high entry requirements imposed on them.

11.4.2 Accounting Profession

It was stated earlier that the development of the accounting profession hinges very much on an effective professional body. Thus, in order to improve the accounting profession in Saudi Arabia, the following are recommended:

1. A Saudi Institute of Certified Accountants should be created. Such an institute could ensure that individuals practising public accounting have the necessary accounting competence; determine the minimum level of accounting and other education required prior to

taking the qualifying examination; determine the practical experience requirement for obtaining a licence to practise public accounting; advocate accounting research leading to the continued improvement of accounting and auditing practices; and represent the country in any international accounting conferences, surveys or comparative studies.

2. Public accountants in Saudi Arabia should widen their services to include effectiveness and efficiency audit, and feasibility studies. Such services are now needed more than ever, because the financial situation of the country is not as it was a few year ago. The Kingdom now faces a shortage of funds and the available resources should be used more economically.

3. Public accountants in Saudi Arabia should cooperate with local academic institutions, particularly with regard to the type of training programmes needed for local accountants in order to enhance the level of services rendered.

4. The members of the "Higher Committee of Certified Accountants" need to play a more active role in the development of the profession.

5. Local accountants should increase their contribution in any future move toward the development of the accounting profession in Saudi Arabia.

11.4.3 Enterprise Accounting

In order to improve enterprise accounting in Saudi Arabia, the following recommendations are made:

1. A certain degree of consistency in accounting rules, policies, formats, classifications and reporting procedures is badly needed.

2. The accounting techniques for planning and control should be emphasised.

3. More accounting data related to national accounting, value added, social responsibility and other non-financial information should be disclosed either in the main body of financial reports or in supplementary statements.

4. Accountants in these enterprises should receive regular training in the latest accounting techniques and procedures.

5. Given the absence of statutory requirements, now is perhaps the appropriate time to study the possibility of linking published financial reports with national accounts, so that the information produced by the former can become a component of the information input to the latter.

11.4.4 Government Accounting

In order to improve the government accounting in Saudi Arabia, the following are recommended:

1. The lengthy procedures currently applied in the public sector units should be cut down and simplified.

2. The accounting principles, classifications, formats and reporting procedures among the government units should be unified and updated.

3. All government units should be encouraged to use electronic data processing to handle their financial transactions.

4. The scope of audit should be expanded to include measurements of the efficiency, economy, and effectiveness of public expenditure.

5. A sound programme structure must be established, whereby the budget classifications are related closely to projects included in the five-year development plan.

11.4.5 National Accounting

In order to improve national accounting to serve effectively the development planning process in Saudi Arabia, the following are recommended:

1. Cooperation between accountants in industry, the accounting profession, and CDS staff must be established to collect the necessary data required for national accounts.

2. The surveys of establishments should be extended to cover all economic units, including medium and small units.

3. The forms designed by the CDS for collecting data for national accounts should be amended to generate more relevant data. Moreover, these forms should be accompanied by guidelines explaining how they should be

completed and assuring the respondents that such data will remain confidential.

4. Government units should cooperate with the CDS by sending their final accounts and other related reports on a regular and timely basis.

5. Linkages between the micro and the macro accounting systems should be established. Thus the accounting systems (formats, classifications, policies and procedures) of individual economic units should be designed to produce accounting information relevant to the construction of national accounts. The greater the conformity between enterprise and government accounts and the classifications used for the national accounts, the easier it will be to construct the national accounts, and the better will be their quality.

6. National accounting should be included in the accounting programmes currently offered by Saudi universities, so that accounting graduates are equipped with basic knowledge of this vital subject.

7. The training period of national accounts staff may have to be extended to two years or more to enable trainees to acquire sufficient knowledge and experience in the field of national accounts.

8. A computer network should be established between the CDS headquarters and its branches throughout the Kingdom on the one hand, and other economic units on the other, to generate better and more timely accounting data.

In order to put the above recommendations into practice and to improve the overall accounting system in Saudi Arabia, a comprehensive accounting development plan has been suggested (see chapter 10). The plan is based upon the socio-economic development needs of Saudi Arabia, which require an urgent improvement of all accounting system components (education, profession, enterprise, government and national accounting) simultaneously, by integrating them into a single framework of action.

The plan assumes the willingness of accounting academicians, public accountants, and government officials, particularly those involved in planning, implementation, and control of the economic and financial activities of the country, to participate in the accounting improvement process. Moreover, the suggested plan should be viewed as a part of the overall five-year economic development plan which already exists.

Although the emphasis throughout this thesis has been placed upon the Saudi Arabian environment, it is hoped that other developing countries will benefit from this study. In particular, the GCC countries, which have similar environments to that of Saudi Arabia, may be encouraged to broaden their development efforts toward vital areas of accounting such as education and training, public sector accounting, and national accounting, instead of concentrating upon only one area (i.e. external financial reporting) which may be of relatively

little importance for their socio-economic environment. It is also hoped that this study will go some way towards filling the existing gap in the literature concerning the status of accounting systems in developing countries and contribute to a better understanding of their accounting problems.

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APPENDICES

Appendix (A) Public Accountants' Questionnaire

Part I --> General data

This part is designed to gather general data concerning the respondent's background (e.g. his current position in the firm, education level, place of education, number of years experience etc).

- 1) Which one of the following describes your position in your firm?
 - a. Owner [42%]
 - b. Partner [28%]
 - c. Accountant in charge [23%]
 - d. Other (please specify) [07%]

- 2) Which one of the following describes your highest educational qualification?
 - a. Bachelor Degree (major accounting) [52%]
 - b. Bachelor Degree (major business administration) [37%]
 - c. Master Degree [09%]
 - d. Ph.D Degree [02%]
 - e. Other (please specify) [Nil]

- 3) Where did you receive your highest education?
 - a. Saudi Arabia [73%]
 - b. Arab country (please specify) [19%]
 - c. Foreign country (please specify)..... [08%]

- 4) Do you have accounting work experience?

Yes	[100%]
No	[Nil]

- 5) If your answer to question 4 is "Yes", please check the following:
 - a. Less than 5 years [13%]
 - b. Between 5 years to 10 years [67%]
 - c. More than 10 years [20%]

- 6) Please specify the place in which the experience referred to in question 5 took place?
- | | |
|----------------------------------|-------|
| a. Accounting Firm | [47%] |
| b. Government Department | [39%] |
| c. Private Business | [35%] |
| d. Bank | [27%] |
| e. Others (please specify) | [Nil] |
- 7) Does your work involve use of the computer?
- | | |
|----------------|-------|
| Yes | [17%] |
| No | [51%] |
| To some extent | [32%] |
- 8) Do you have any professional title from any accounting society?
- | | |
|-----|-------|
| Yes | [10%] |
| No | [90%] |
- 9) If the answer to question 8 is "yes", please indicate the name of the society and country of origin?
- 10) How do you evaluate the level of new accounting graduates who apply to practice in your firm as accountant under-training?
- | | |
|-------------|-------|
| a. Good | [23%] |
| b. Adequate | [56%] |
| c. Weak | [21%] |

Part II --> Accounting Standards in Practice

The aim of this part is to obtain the public accountants' opinion concerning the accounting standards widely used in Saudi Arabia, the reasons for this, the main problems facing them when they audit the financial statements of Saudi Corporations. It also aims to gather information concerning types of services rendered.

- 11) According to your experience as a public accountant, what type of accounting standards are widely used in Saudi Arabia?
- | | |
|--|-------|
| a. International Accounting Standards (IASs) | [44%] |
| b. American Accounting Standards | [30%] |
| c. British Accounting Standards | [19%] |
| d. Other (please specify) | [7%] |

- 12) What do you think are the main reasons behind the spread of this type of Standards in Saudi Arabia?
- | | |
|--|-------|
| a. Non existence of local accounting standards | [62%] |
| b. Accountants' education and experience | [28%] |
| c. Spread of International Accounting Firms' Branches in Saudi Arabia? | [22%] |
| d. Other (please specify) | [Nil] |
- 13) Do you think that any of the accounting standards referred to in question 11 above are relevant to the socio-economic environment of Saudi Arabia?
- | | |
|-------------|-------|
| Yes | [Nil] |
| No | [93%] |
| Do not know | [07%] |
- 14) Have you ever worked as an external auditor to any of Saudi corporations?
- | | |
|-----|-------|
| Yes | [76%] |
| No | [24%] |
- 15) If the answer to question 14 is "yes", in your opinion what is/are the main problem(s) that these enterprises suffer from?
- | | |
|--|-------|
| a. Shortages of qualified accountants | [48%] |
| b. Weakness of internal control system | [34%] |
| c. Application of diverse accounting Standards | [13%] |
| d. Combination of a, b and c | [06%] |
- 16) Do you think the adoption of a uniform accounting system (i.e unified accounting formats, methods, rules, principles etc) would alleviate the problems currently facing these enterprises?
- | | |
|-----|-------|
| Yes | [73%] |
| No | [27%] |
- 17) If the answer to question 16 is "yes", who you think should establish and enforce such a system?
- | | |
|--|-------|
| a. Team including representatives of the accounting profession, accounting academics, and government officials | [47%] |
| b. Government agency such as the Ministry of Trade | [28%] |
| c. Private accounting body | [25%] |
| d. Other (please specify) | [Nil] |

18) Please place in rank order from 1-6 the following services, using 1 to indicate the services which accounts for the greatest proportion of your firm's operation, and 6 for the services least performed by your firm?

a. Auditing	[1]	[74%]
b. Income Tax and Zakat	[2]	[58%]
c. Book-keeping	[3]	[43%]
d. Solvency and Liquidation	[4]	[24%]
e. System Design and Installation	[5]	[16%]
f. Management Services	[6]	[10%]

Part III --> Recent Accounting Guidelines

The aim of this part is to seek the public accountants' opinions concerning the recent accounting development in Saudi Arabia which have resulted in the publication of some accounting and auditing guidelines.

19) As you know, setting accounting standards in any country is primarily the responsibility of the profession, with participation from other interested parties. Have you or any accountant of your firm participated in this project?

Yes [02%]
No [98%]

20) If the answer to question 19 is "yes", please indicate in which of the following stages do you participated?

a. Determination of financial accounting objectives	[Nil]
b. Selection of the main financial accounting concepts	[Nil]
c. Preparation of general standard for disclosure and presentation	[Nil]
d. Preparation of auditing standards	[02%]
e. Internal organization of the profession	[Nil]

21) If the answer to question 19 is "no", have you seen the contents of the accounting and auditing standards established so far?

Yes [75%]
No [25%]

- 22) If the answer to question 21 is "Yes", what is your opinion about these standards?
- a. They are similar to the UK and USA standards [57%]
 - b. They are long and contain unnecessary detail [23%]
 - c. They concentrate on external financial reporting and external auditing [20%]
 - d. Other (please specify) [Nil]

- 23) As you know, that these standards were promulgated by the Minister of Commerce's order No. 692 dated 28/2/1406H (1986) as guidelines for the public accountants licensed to practise in Saudi Arabia, and they were put under trial for a period of two years after which they would become mandatory. However, now four years have passed and to the best of the researcher's knowledge they have still not been made mandatory despite, the need for them, as indicated in the project draft. What do think are the main reasons for such delay?
- a. Lack of enforcement body [64%]
 - b. Lack of institutional support [48%]
 - c. Lack of cooperation from interested parties [19%]
 - d. Do not know [15%]

- 24) Did you participate in any of the meetings held to discuss the future of these standards?
- Yes [30%]
No [70%]

- 25) Have you met with other accountants to discuss the contents of these standards and other matters related to the development of accounting profession in Saudi Arabia?
- Yes [07%]
No [93%]

26) Undoubtedly, establishing accounting standards in any country is not an easy task because of the cost, effort and time involved. The task, of course, does not end with the mere establishing of the standards, because they need to be followed up and amended if necessary. Since there is no professional body in Saudi Arabia and even the accounting institute recommended in the project has yet to be established, do you think it would be better to wait rather than establishing more standards?

- a. Agree [51%]
- b. Disagree [29%]
- c. No opinion [20%]

27) Do you have any suggestion concerning the development of the accounting profession in Saudi Arabia?

- Yes [40%]
- No [60%]

28) If your answer to question 27 is "yes", please write down your suggestion in the space provided below.

Appendix (B): Industrial Enterprises' Questionnaire

Part I --> General data

This part is designed to gather general data concerning the enterprise under investigation and the respondent's educational background.

- 1) Name of the enterprise:
- 2) Date of establishment:
- 3) Location
- 4) Number of branches (if any)
- 5) The main activities:.....
- 6) Respondent's citizenship:
 - a. Saudi [19]
 - b. Non-Saudi [06]
- 7) Level of education:
 - a. Less than Bachelor Degree [00]
 - b. Bachelor Degree [21]
 - c. Master Degree [04]
 - d. Other (Higher Diploma in Cost Accounting) [01]
- 8) Place of education:
 - a. Saudi Arabia [12]
 - b. Arab country (mainly Egyptian) [10]
 - c. Foreign country (mainly USA and UK) [03]
- 9) Experience in accountancy and finance:
 - a. Less than 3 years [02]
 - b. Between 3 years to 5 years [05]
 - c. More than 5 years [18]
- 10) How do you perceive the role of accounting in your enterprise?
 - a. Very important [23]
 - b. Important [02]
 - c. Not very important [00]
 - d. Insignificant [00]

Part II --> Features of accounting system and practice

The purpose of this part is to examine the current accounting recording, reporting procedures and methods used by Saudi industrial corporations.

[A] General Features

- 11) Who designed the accounting system of your enterprise?
- a. Accountants of the enterprise [8]
 - b. Saudi accounting firm [5]
 - c. Foreign accounting firm [9]
 - d. Other (please specify) [3]
- 12) How do you process data in your enterprise's accounting system?
- a. Manual [03]
 - b. Mechanical [04]
 - c. Computer [06]
 - d. Combination of a, b and c [12]
- 13) Does the enterprise have a chart of accounts?
- Yes [10]
 - No [15]
- 14) What types of financial report do you presently prepare?
- a. Balance Sheet [25]
 - b. Profit and Loss [25]
 - c. Director's Report [25]
 - d. Source and Application of Funds Statement [08]
 - e. Changes in Financial Position Statement [05]
 - f. Other (please specify) [00]
- 15) How often are financial reports prepared in your enterprise?
- a. Annually [25]
 - b. Semi-annually [00]
 - c. Quarterly [25]
 - d. a and c [25]
- 16) Do you publish information additional to the financial reports?
- Yes [04]
 - No [21]

- 17) Do you seek any assistance from outside auditors or accountants when preparing financial reports?
- | | |
|-----|------|
| Yes | [05] |
| No | [20] |
- 18) Does the enterprise publish its financial reports in local newspapers?
- | | |
|-----|------|
| Yes | [25] |
| No | [00] |
- 19) Do you always disclose the accounting policies used in the preparation of financial reports?
- | | |
|-----|------|
| Yes | [13] |
| No | [12] |
- 20) To the best of your knowledge, who do you think use the financial reports of your enterprise?
- | | <u>Rank</u> | <u>No.</u> |
|---------------------------------------|-------------|------------|
| a. Owners (shareholders) | [1] | [21] |
| b. Department of Zakat and Income Tax | [2] | [20] |
| c. Saudi Industrial Development Fund | [3] | [18] |
| d. Commercial Banks | [4] | [16] |
| e. Ministry of Commerce | [5] | [12] |
| f. Employees | [6] | [08] |

[B] Accounting Reporting and Practice

- 21) What basis is usually used by the enterprise for Stock evaluation?
- | | |
|----------------------------------|------|
| a. Cost basis | [09] |
| b. Market price | [00] |
| c. Lower of cost or market price | [16] |
| d. Other (please specify) | [00] |
- 22) Which method is usually used by the enterprise for depreciation of fixed assets?
- | | |
|---------------------------------|------|
| a. Straight-line | [21] |
| b. Reducing Balance | [03] |
| c. Percentage of use | [01] |
| d. Other (please specify) | [00] |
- 23) In determining the cost of inventory, which method is generally used by the enterprise?
- | | |
|---------------------------------|------|
| a. First in, first out (FIFO) | [18] |
| b. Weighted Average | [07] |
| c. Last in, first out (LIFO) | [00] |
| d. Other (please specify) | [00] |

- 24) Is the concept of matching cost and revenue in measuring income used by your enterprise?
Yes [25]
No [00]
- 25) Which basis of accounting is mostly used by your enterprise?
a. Accrual basis [25]
b. Cash basis [00]
c. Other (please specify) [00]
- 26) At what point are revenues realized in your enterprise?
a. Completion of production point [02]
b. Sales point [17]
c. Delivery point [06]
d. Other (please specify) [00]
- 27) Does the enterprise have a programme for Research and Development (R&D)?
Yes [05]
No [20]
- 28) If the answer to question (27) is yes, how do you treat the expenses of such programme?
a. charge all the expenses of R&D to the period in which they are incurred. [3]
b. capitalise all expenses of R&D as assets when incurred [2]
c. other (please specify) [0]
- 29) Does the enterprise have any type of accounting for foreign currency translation?
Yes [06]
No [19]
- 30) If the answer to question (29) is yes, what is the approach used for foreign currency translation?
a. historical cost rate [00]
b. current exchange rate [19]
c. other [00]
- 31) Does the enterprise have any type of accounting for inflation?
Yes [03]
No [22]

- 32) If the answer to question (31) is yes, what is the approach used for inflation accounting?
- a. general purchasing power [0]
 - b. replacement cost [2]
 - c. current cost accounting [1]
 - d. other (please specify) [0]
- 33) What are your sources of accounting methods, policies, rules, and principles?
- a. Written accounting system [02]
 - b. Personal experience [01]
 - c. Various laws and regulations [01]
 - d. Combination of a, b, and c [21]
- 34) Has the enterprise changed its accounting system during the last five years?
- Yes [11]
No [14]

[C] Accounting for Planning and control

- 35) Do you use a budgeting system for the purpose of planning and control?
- Yes [23]
No [02]
- 36) If the answer to question (35) is yes, please indicate which of the following budgets are included in your budgeting systems.
- a. Production budget [21]
 - b. Sales budget [02]
 - c. Purchases budget [18]
 - d. Capital expenditures budget [16]
 - e. Cash budget [16]
 - f. Administration budget [07]
 - h. Other (please specify) [00]
- 37) Is there a long-term plan designed to ensure that all objectives are attained over a period?
- Yes [16]
No [09]
- 38) What method do you normally use for long-term capital expenditure decision?
- a. Pay back method [17]
 - b. Discount cash flow [05]
 - c. Accounting rate of return [02]
 - d. Other [depends on outsider consultant body] [01]

- 39) Do you use the standard costing technique whereby standard cost and selling price are predetermined and subsequently compared with actual recorded cost and revenues?
- Yes [09]
No [16]
- 40) Do you calculate and analyse the variances resulting from the use of such technique?
- Yes [09]
No [16]
- 41) If the answer to question (40) is yes, please indicate which of the following variances are calculated?
- a. Materials Variance [04]
b. Labour Variance [02]
c. Overheads Variance [03]
d. Other [01]
- 42) Do you carry out any other form of cost analysis, such as break-even point analysis?
- Yes [11]
No [14]
- 43) Do you break down the total costs into fixed costs and variable costs?
- Yes [13]
No [12]

Part -> III Enterprise Accounting System and Its Relationship to National Accounts

The purpose of this part is to survey the contribution of the current accounting system and practice at enterprise level in providing accounting information relevant to the construction of national income accounts in Saudi Arabia.

Based on your knowledge and practice in your enterprise, please answer the following questions by ticking the appropriate box.

- 44) Do the accounts of your enterprise have any link with national income accounts?
- Yes [03]
No [22]

- 45) Do the government agencies responsible for national planning (such as Ministry of Planning and CDS) require you to submit information in addition to that contained in the financial statements?
- Yes [06]
No [19]
- 46) If the answer to question (45) is yes, how frequently is such information required?
- a. Annually [6]
b. Smi-annually [0]
c. Quarterly [0]
- 47) Are the accountants in your enterprise aware of the accounting information needs of national accounts?
- Yes [05]
No [20]
- 48) If the answer to question (47) is No, what do you think is the main reason?
- a. because there is no statutory requirement for information needed by national accounts [12]
b. because the existing accounting system of the enterprise is not designed to provide such information [08]
c. because we do not have qualified accountants for this purpose [05]
d. Other (please specify) [00]
- 49) If the answer to question (47) is Yes, please indicate which of the following items are disclosed, either in the main body of the financial reports or in supplementary reports.

Items	Yes	No
1> various components of fixed assets	7	18
2> details relating to historical cost - year of purchase - new or second hand acquisition - depreciation rate - expected life	6	19
3> classification of stock into: - raw materials - work in progress - finished goods	9	16
4> classification of cash between local and foreign currency	4	21
5> classification of long-term investment between foreign and local-based	2	23
6> the amount of imports	7	18
7> the amount of exports	6	19
8> value added and its components	0	25
9> transfer payments	7	18
10> sales of goods to non-residents	6	19
11> salaries and wages paid to non-residents	5	20
12> state subsidies	11	14
13> increase in physical inventory	4	21
14> classification of cash between cash in hand and cash at bank	7	18
15> classification of purchases between purchase for sales and purchase for use	3	22

50) Does your enterprise disclose any type of social
and non-financial information?

Yes [06]
No [19]

51) If the answer to question (50) is yes please indicate which of the following are disclosed:

Items	Yes	No
1> Employee welfare	2	23
2> Donations for social causes	1	24
3> Encouragement of use of Saudi employees	3	22
4> Health and safety protection	00	25
5> Pollution control	00	25

Part IV --> Accounting Manpower

This part is designed to survey the enterprise's demand for qualified accountants, and to gather the opinion of the financial managers of the enterprises in question with respect to the possibility of adopting uniform accounting system.

In answering the following questions, you may, if you wish, use the attached sheet, to provide more information.

52) What is the total number of employees in your enterprise?

- a. Less than 200 [03]
- b. Between 200 to 400 [06]
- c. More than 400 [16]

53) Please, indicate the number of Accountants in your enterprise as:

- a. Saudi =204
- b. Non-Saudi =396

54) Does your enterprise face a problem in recruiting a new accountants?

- Yes [17]
- No [08]

- 55) If the answer to question (54) is yes, please indicate the extent to which the following accounting fields need qualified personnel in your enterprise, ranking them from 1, for the field which most needs these personnel, to 5 for the field which has least need:
- a. Financial Accounting [18]
 - b. Auditing [15]
 - c. Cost and Managerial Accounting [13]
 - d. Specialized and Applied Accounting [09]
 - e. Taxation and Zakat Accounting [05]
- 56) Do you provide any type of training for these new accountants?
- Yes [07]
 - No [18]
- 57) If the answer to question (56) is yes, please indicate the methods of training?
- a. Overseas training programme [0]
 - b. Local training Institution [5]
 - c. Own training centre [2]
- 58) Do you have any knowledge of the recent development of accounting and auditing standards in Saudi Arabia?
- Yes [08]
 - No [17]
- 59) Would you recommend the adoption of a uniform accounting system (i.e unified accounting formats, methods, rules, principles etc) to be applied by Saudi Public enterprises?
- Yes [19]
 - No [06]
- 60) If the answer to question (59) is yes, who do you think should establish and enforce such a system?
- a. Team including representatives of the accounting profession, accounting academics, and government officials [11]
 - b. Government agency such as the Ministry of Commerce [06]
 - c. Private accounting body [02]
 - d. Other (please specify) [00]

Appendix (C) List of Interviewees

1. Abdul Gafor, M., General Director of the Department of Zakat and Income Tax (DZIT).
2. Al-Ali, A., Specialized National Accounts, Central Department of Statistics.
3. Al-Amar, A., Head of the General Accounts Section, the Ministry of Finance and National Economy.
4. Al-Drise, M., General director of the National Information Centre.
5. Al-Otabi, M., General Director of the Companies Department, Ministry of Commerce.
6. Al-Gamdi, A., Companies Department, the Ministry of Commerce.
7. Al-Hakmi, A., Assistant Deputy Minister for Sectors Planning, the Ministry of Planning.
8. Al-Jarallah, A., Director of the Financial Representative Administration.
9. Al-Molhem, S. A., Senior Accountant in the DZIT.
10. Al-Muhana, M., National Accounts Consultant, Central Department of Statistics.
11. Al-Rashed, A., Managing partner of Al-Rashed Certified Public Accountants.
12. Al-Saad, A., Director of National Accounts Administration, Central Department of Statistics.
13. Aziz, A. A., Financial Consultant, Ministry of Finance and National Economy.
14. ABu-hamed, A., Vice President of the GAB.
15. Jameel, A., Assistant Deputy Minister and the current chairman of the "Higher Committee of Charter Accountants".
16. Jamjoom, A., Director of Financial Affairs, the Department of Zakat and Income Tax.
17. Najeep, M., Secretary of Saudi Accounting Association
18. Nasrallah, A., Assistant Deputy Minister for Financial Affairs and Accounts.
19. Salem, A., Senior Accountant, Companies Department.
20. Tawfeeg, G., Budget Department, Ministry of Finance.

Appendix D Illustrative Forms of Financial Statements

First: Illustrative Forms of the Balance Sheet.

Form A
Vertical, Classified, and Comparative Balance Sheet
Arab Company - Joint Stock Company

Balance Sheet as of 00/00/14X2 H.

<u>14X1 H.</u>				<u>14X2 H.</u>	
<u>Riyal</u>	<u>Riyal</u>	<u>Current Assets</u>	<u>Note</u>	<u>Riyal</u>	<u>Riyal</u>
	XX	Cash on hand and in banks	()	XX	
	XX	Accounts Receivable	()	XX	
	XX	Merchandise inventory	()	XX	
	XX	Prepaid expenses	()	XX	
	XX		()	XX	
	<u>XX</u>		()	<u>XX</u>	
XXX		Total Current Assets			XXX
		<u>Current Liabilities</u>			
	XX	Notes payable	()	XX	
	XX	Accounts Payable	()	XX	
	XX	Accrued expenses	()	XX	
	XX	Dividends Payable	()	XX	
	XX	Current portion of long-term loan	()	XX	
	XX	Zakat (income tax) payable	()	XX	
	XX		()	XX	
	<u>XX</u>		()	<u>XX</u>	
<u>(XXX)</u>		Total Current Liabilities			<u>(XXX)</u>
XXX		Working capital			XXX
		<u>Fixed Assets</u>			
	XX	Land	()	XX	
	XX	Buildings	()	XX	
	XX	Machines & equipment	()	XX	
	XX	Office furniture & tools	()	XX	
	XX	Accumulated depreciation	()	XX	
	<u>XX</u>		()	<u>XX</u>	
XXX		Total Fixed Assets			XXX

Intangible Assets

	XX	Patents	()	XX	
	XX	Goodwill	()	XX	
	XX		()	XX	
	<u>XX</u>		()	<u>XX</u>	
<u>XXX</u>		Total Intangible Assets			<u>XXX</u>
XXX					XXX

NonCurrent Liabilities

	XX	Long-term debts	()	XX	
	XX	Accrual for end-of-service benefits	()	XX	
	XX		()	XX	
	<u>XX</u>		()	<u>XX</u>	
<u>(XX)</u>		Total Noncurrent Liabilities			<u>(XXX)</u>
XXX					XXX
===					===

Owners' Equity

		Authorized capital ____ shares at nominal value ____ riyals			
	XX	per share of stock	()	XX	
		Less: Nonissued capital			
	<u>(XX)</u>	____ shares	()	<u>(XX)</u>	
XX		Paid-up Capital			XX
	XX	Capital Grants	()	XX	
	XX	Reserves or appropriated retained earnings		XX	
				XX	
	<u>XX</u>			<u>XX</u>	
XX		Total Owners' Equity			XX
<u>XX</u>		Contingent Liabilities	()		<u>XX</u>
XXX					XXX
===					===

Attached notes from No. () to No. () form an integral part of the financial statements.

- ** Balance sheet item.
*** Balance sheet group.

Form B
Horizontal, Classified and Comparative Balance Sheet
Arab Company - Joint Stock Company

Balance Sheet as of 00/00/14X2 H.

	<u>Note</u>	<u>14X2 H.</u>	<u>14X1 H.</u>	<u>14X2 H.</u>	<u>14X1 H.</u>
		<u>Riyal</u>	<u>Riyal</u>	<u>Riyal</u>	<u>Riyal</u>
<u>Current Assets:</u>					
Cash on hand & in banks	()	xx	xx	xx	xx
Accounts rec'ble	()	xx	xx	xx	xx
Merchandise inventory	()	xx	xx	xx	xx
Prepaid expenses	()	xx	xx	xx	xx
_____	()	xx	xx	xx	xx
_____	()	xx	xx	xx	xx
_____	()	xx	xx	xx	xx
_____	()	xx	xx	xx	xx
<u>Total Current Assets</u>	()	xxx	xxx	xxx	xxx
<u>Fixed Assets:</u>					
Land	()	xx	xx	xx	xx
Buildings	()	xx	xx	xx	xx
Machines and equipment	()	xx	xx	xx	xx
Office furniture and tools	()	xx	xx	xx	xx
Accumulated depreciation	()	(xx)	(xx)	(xx)	(xx)
<u>Total Fixed Assets</u>	()	xxx	xxx	xxx	xxx
<u>Current Liabilities:</u>					
Notes payable	()			xx	xx
Accounts payable	()			xx	xx
Accrued expenses	()			xx	xx
Dividends payable	()			xx	xx
Current portion of long-term loans	()			xx	xx
Zakat (income tax) payable	()			xx	xx
_____	()			xx	xx
_____	()			xx	xx
<u>Total Current Liabilities</u>	()			xxx	xxx
<u>Noncurrent Liabilities:</u>					
Long-term loans	()			xx	xx
Accrual for end-of-service benefit	()			xx	xx
<u>Owners' Equity:</u>					
Authorized capital					
...shares at nominal value					
.....					
riyals per share of stock	()			xx	xx

Intangible Assets:

Patents	()	xx
Goodwill	()	xx
	()	xx
	()	xx
<u>Total Intangible Assets</u>		<u>xxx</u>
Total Assets		xxx
		===

Less: issued capital ...shares()	(xx)	(xx)
Issued & paid-up capital	xxx	xxx
Capital grants	xx	xx
Reserves or appropriated retained earnings	xx	xx
Nonappropriated retained earnings()	xx	xx
	xx	xx
	xx	xx
<u>Total Owners' Equity</u>	xxx	xxx
Contingent Liabilities	xx	xx
Total Liabilities and Owners' Equity	xxx	xxx
	===	===

Attached Notes from No. () to No. () form an integral part of the financial statements.

** Balance sheet item.
 *** Balance sheet group.

Form C

Horizontal, Unclassified and Comparative Balance Sheet
Arab Company - Joint Stock Company

Balance Sheet as of 00/00/14X2 H.

	Note	14X2 H. Riyal	14X1 H. Riyal	Note	14X2 H. Riyal	14X1 H. Riyal
Cash on hand and in banks	()			()	xx	xx
Accounts Rec'ble	()	xx	xx	()	xx	xx
Notes receivable	()	xx	xx	()	xx	xx
Prepaid expenses		xx	xx		xxx	xxx
Land	()					
Buildings	()	xx	xx			
Furniture	()	xx	xx			
Accumulated depreciation	()	(xx)	(xx)	()	xx	xx
Goodwill	()	xxx	xxx			
Patents	()	xx	xx	()	(xx)	(xx)
Total Assets		xxx	xxx		xxx	xxx
Notes payable	()			()	xx	xx
Accounts Payable	()	xx	xx	()	xx	xx
Accrued expenses	()	xx	xx	()	xx	xx
Owners' Equity:						
Authorized capital						
_____ shares at nominal value						
_____ riyals per share of stock						
Less: nonissued capital						
_____ shares _____						
Issued & paid-up capital	()	xx	xx	()	(xx)	(xx)
Capital grants	()	xxx	xxx	()	xx	xx
Reserves or appropriated retained earnings	()	xxx	xxx	()	xx	xx
Nonappropriated retained earnings	()	===	===	()	xx	xx
Contingent Liabilities	()	xxx	xxx	()	xxx	xxx
Total Liabilities and Owners' Equity		===	===		xxx	xxx

Attached Notes from No. () to No. () form an integral part of the Financial Statements

** Balance sheet item.
*** Balance sheet group.

Second: Illustrative Forms of the Income Statement.

Form A
Income Statement
(Continuing Operations and Extraordinary Items)
Arab Company - Joint Stock Company

Income Statement for the year ended 00/00/14X2 H.

<u>14X1 H.</u>				<u>14X2 H.</u>	
<u>Riyal</u>	<u>Riyal</u>		<u>Note</u>	<u>Riyal</u>	<u>Riya</u>
	xx	Net sales	()	xx	
	<u>xx</u>	Cost of sales	()	<u>xx</u>	
xxx		Gross profit			xxx
		<u>Expenses of Continuing Operations</u>			
	xx	Sales expenses	()	xx	
	xx	General & Administrative expenses	()	xx	
<u>xxx</u>					<u>xxx</u>
xxx		Income from continuing operations			xxx
		<u>Results of Other Operations</u>			
	xx	Net rentals	()	xx	
	xx	Investment revenues	()	xx	
	<u>(xx)</u>	Loss from selling fixed assets	()	<u>(xx)</u>	
<u>xxx</u>					<u>xxx</u>
		Net income before extra-ordinary gains (losses)			xxx
xxx		Extraordinary gains (losses)	()		<u>xxx</u>
<u>xxx</u>		Net income			<u>xxx</u>
===					===

Attached notes from No. () to No. () form an integral part of the financial statements.

** Income Statement Item.

*** Income Statement Group.

Form B
Income Statement
(Continuing Operations, Discontinued Operations and
Extraordinary Items)
Arab Company - Joint Stock Company

Income Statement for the Year Ended 00/00/14X2 H.

<u>14X1 H.</u>			<u>14X2 H.</u>	
<u>Riyal</u>	<u>Riyal</u>	<u>Note</u>	<u>Riyal</u>	<u>Riyal</u>
	xx	Net sales	xx	
	<u>xx</u>	Cost of sales	<u>xx</u>	
xxx		Gross profit		xxx
<u>Expenses of Continuing Operations</u>				
	xx	Sales expenses	xx	
	<u>xx</u>	General & Administrative expenses	()	<u>xx</u>
<u>xxx</u>				<u>xxx</u>
xxx		Income from continuing operations		xxx
<u>Results of Other Operations</u>				
	xx	Net rentals	()	xx
	xx	Investment revenues	()	xx
<u>xxx</u>	<u>(xx)</u>	Losses from fixed asset sales	<u>(xx)</u>	<u>xxx</u>
xxx		Income from continuing operations		xxx
<u>Discontinued Operations</u>				
	xx	Results of discontinued operations		xx
	<u>(xx)</u>	Losses from selling <i>assets of</i> discontinued operations	<u>(xx)</u>	
<u>(xxx)</u>				<u>(xxx)</u>
xxx		Net income before extraordinary losses		xxx
<u>(xxx)</u>		Extraordinary losses		<u>(xxx)</u>
xxx		Net income		xxx
===				===

Attached notes from No. () to No. () form
an integral part of the financial statements.

** Income Statement Item.
*** Income Statement Group.

Form C
 Income Statement
 (Continuing Operations and Operating Subsidy)
 Arab Company - Joint Stock Company

Income Statement for the Year Ended 00/00/14X2 H.

<u>14X1 H.</u>			<u>Note</u>	<u>14X2 H.</u>	
<u>Riyal</u>	<u>Riyal</u>			<u>Riyal</u>	<u>Riyal</u>
	xx	Net sales		xx	
	<u>xx</u>	Cost of sales		<u>xx</u>	
(xxx)		Gross loss			(xxx)
<u>Expenses of Continuing Operations</u>					
	xx	Sales expenses		xx	
	<u>xx</u>	General & Administrative expenses	()	<u>xx</u>	
<u>xxx</u>		Income from continuing operations			<u>xxx</u>
(xxx)					(xxx)
<u>Results of Other Operations</u>					
	xx	Net rentals	()	xx	
	xx	Investment revenues	()	xx	
	<u>(xx)</u>	Loss from selling of fixed assets		<u>(xx)</u>	
<u>xxx</u>		Net loss before operating			<u>xxx</u>
(xxx)		subsidy			(xxx)
<u>xx</u>		Operating subsidy		<u>xx</u>	
xxx		Net income			xxx
===					===

Attached Notes from No. () to No. () form
 an integral part of the financial statements.

- ** Income Statement Item.
 *** Income Statement Group.

Third: Illustrative Form of the Statement of Retained Earnings.

Arab Company - Joint Stock Company

Statement of Retained Earnings
for the Year Ended 00/00/14X2 H.

<u>Unappropriated</u> <u>Retained Earnings</u>	<u>General</u> <u>Reserve</u>	<u>Legal</u> <u>Reserve</u>	<u>Note</u>
<u>Riyal</u>	<u>Riyal</u>	<u>Riyal</u>	
xxx	xxx	xxx	Balance at 00/00/14X1 H. before adjustment.
<u>(xxx)</u>	<u>(xxx)</u>	<u>(xxx)</u>	() Adjustments pertaining to the year ended 00/00/14X0.
xxx	xxx	xxx	Balance at 00/00/14X1 H. after adjustment.
<u>xxx</u>	<u>-</u>	<u>-</u>	Net income for the year ended 00/00/14X2 H
xxx	xxx	xxx	
(xxx)	xxx	xxx	Transfers to reserves
<u>(xxx)</u>	<u>-</u>	<u>-</u>	Dividends
xxx	xxx	xxx	Balance at -1-1 14X1 H
<u>(xxx)</u>	<u>-</u>	<u>-</u>	Net income for the year ended -1-1 14X2 H
xxx	xxx	xxx	
(xxx)	xxx	xxx	Transfers to reserves
<u>(xxx)</u>	<u>-</u>	<u>-</u>	Dividends
=====	=====	=====	Retained Earnings

Attached Notes from No. () to No. () are
an integral part of the financial statements.

Fourth: Illustrative Form of the Statement of Changes in Owners' Equity.

Arab Company - Joint Stock Company

Statement of Changes in Shareholders' Equity for the Years Ended 30 DulHujjah 14X2 H. and 14X1 H.

<u>Unappropriated Retained Earnings Riyal</u>	<u>General Reserve Riyal</u>	<u>Legal Reserve Riyal</u>	<u>Capital Grants Riyal</u>	<u>Pain-In Capital Riyal</u>	<u>Note</u>
xxx	xxx	xxx	xxx	xxx	Balance at 30 DulHijjah 14X0 H. before adjustments
(xxx)	(xxx)	(xxx)	-	-	() Adjustments relating to 14X0 H.
xxx	xxx	xxx	xxx	xxx	Balance at 30 DulHijjah 14X0 H. after adjustments
-	-	-	-	xxx	Issuance of 1000 shares of capital stock.
xxx	-	-	-	-	Net income for the year 14X1 H.
(xxx)	xxx	xxx	-	-	Transfers to reserves.
-	-	-	xxx	-	() Value of land granted for building a factory.
(xxx)	-	-	-	-	Dividends.
xxx	xxx	xxx	xxx	xxx	Balance at 30 DulHijjah 14X1 H.

xxx	-	-	-	-	Net income for the year 14X2 H.
(xxx)	xxx	xxx	-	-	Transfers to reserves.
<u>(xxx)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	Dividends.
<u>xxx</u>	<u>xxx</u>	<u>xxx</u>	<u>xxx</u>	<u>xxx</u>	Balance at 30 DulHijjah 14X2 H.

Attached Notes from No. () to No. () form an integral part of the financial statements.

Applications of working capital:

xx	Settlement of long-term loans	xx
xx	Dividends	xx
xx	Zakat taxes	xx
<u>xx</u>	Purchase of fixed assets	<u>xx</u>
<u>xx</u>	Total applications of working capital	<u>xx</u>
(xx)	Increase (decrease) in working capital	xx
==		===

Other investing and financing activities:

—	Issuance of capital stock to acquire land	xx
—	Acquisition of land by issuing capital stock	(xx)
		====

Attached notes from No. () to No. () form an integral part of the financial statements.

Applications of working capital:

xx	Settlement of long-term loans	xx
xx	Dividends	xx
xx	Zakat taxes	xx
<u>xx</u>	Purchase of fixed assets	<u>xx</u>
xx	Increase in working capital	xx
=====		===

Other investing and financing activities:

—	Issuance of capital stock to acquire land	xx
—	Acquisition of land by issuing capital stock	(xx)
		=====

Attached Notes from No. () to No. () form an integral part of the financial statements.

Applications of Cash:

xx	Repayment of long-term loans	xx	
xx	Dividends	xx	
xx	Purchase of fixed assets	xx	
<u>xx</u>	Zakat taxes	<u>xx</u>	
<u>xx</u>	Total application of cash		<u>xx</u>
(xx)	Increase (decrease) in cash		xx
====			====
	Other investing and financing activities:		
—	Issuance of capital stock to acquire land	xx	
—	Acquisition of land by issuing capital stock	(xx)	
====		====	

Attached Notes from No. () to No. () form an integral part of the financial statements.