Examining the Relationship between Company’s Features and Quality of Financial Reporting in the Listed Companies at Tehran Stock Exchange

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ABSTRACT: The purpose of this study was to examine the relationship between company’s features and quality of financial reporting. The features included profitability, liquidity and rate of sales growth. The model of Francis et al has been used to measure quality of financial reporting. To test hypotheses, there were selected 130 companies in period 2008-2012 by randomly sampling. The present research was applicable objectively.

Keywords: Profitability, Liquidity, Rate of Sales Growth, Quality of Financial Reporting.

INTRODUCTION

Users of financial statements make decisions such as selling; maintain investment in business unit, re-election or replacing managers. Therefore, to take such economic decisions, they should be able to assess power of to generate cash and its time and certainty. In fact, it is ability of a business unit to generate cash that shows its capacity to do payables such as salaries and benefits to employees, payments to suppliers of goods and services, paying financial costs and distributing benefits between capital owners. According theoretical concepts of financial reporting in Iran, focusing on financial position, financial performance and cash flow of a business unit and use them to forecast the expected cash flows as well as assess its financial flexibility facilitate evaluating ability of business unit to create cash, time and certainty (Saghafi & Kurdistan, 2004).

Thus, investors have always been interested to quality of financial reporting (financial statements). Shareholders, as the most important user group of information of financial statements, seek their benefits on profit data. Accounting profit is a sign that will change beliefs and behaviors of investors. Quality of financial reporting can affect trust of investors in financial markets. The most important factors affecting quality of financial reporting include various methods of accounting, failures on assessing and forecasts processes, managers’ independence, profit influencing by reporting basics and managers’ discretion (Dechow, 1994).

The term of quality of financial reporting refers to ability of managers to use optional items to measure and reporting profits. Optional items may include selecting and applying accounting principles or standards and transactions’ schedule to identify the abnormal items in profit (Hashimi & Doy, 2008). During the last three decades, researchers have been interested to quality of financial reporting and they have attempted to evaluate quality of earnings and identify factors affecting it by achieving a reasonable and credible manner (Jugy et al., 2007). Due to the contents, the question is on the relationship between company features and quality of financial reporting, which this study examines the above-mentioned issue.
METHODOLOGY

The research method is correlation in terms of nature and content, which it is one of descriptive researches. In this study, we firstly examined the correlation between variables. If there is correlation between the variables, we will estimate multiple regression models. In the other hand, the study is post-event (semi-experimental), i.e. it is carried out based on analyzing historical and previous data (corporate financial statements). It is also a library study and analytical-casual research based on panel data analysis. The following research model is used to measure hypotheses test:

\[
\text{The research model: } FRQ_{it} = \beta_0 + \beta_1 \text{SIZE}_{it} + \beta_2 \text{LEV}_{it} + \beta_3 \text{COMP}_{it} + \beta_4 \text{IS}_{it} + \varepsilon_{it}
\]

The model for quality of financial reporting (Francis et al):

\[
\Delta \text{WC}_{it} = \beta_0 + \beta_1 \text{CFO}_{it-1} + \beta_2 \text{CFO}_{it} + \beta_3 \text{CFO}_{it+1} + \beta_4 \Delta \text{REV}_{it} + \beta_5 \text{PPE}_{it} + \varepsilon
\]

<table>
<thead>
<tr>
<th>Description</th>
<th>Coefficient</th>
<th>t-statistics</th>
<th>Sig.</th>
</tr>
</thead>
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<tr>
<td>C</td>
<td>3.51</td>
<td>6.4</td>
<td>0.000*</td>
</tr>
<tr>
<td>PROF</td>
<td>0.42</td>
<td>2.9</td>
<td>0.003*</td>
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<tr>
<td>LIQ</td>
<td>0.33</td>
<td>3.88</td>
<td>0.000*</td>
</tr>
<tr>
<td>GROWTH</td>
<td>0.04</td>
<td>5.94</td>
<td>0.000</td>
</tr>
<tr>
<td>C</td>
<td>3.51</td>
<td>6.4</td>
<td>0.000*</td>
</tr>
</tbody>
</table>

Results of the table show that significant statistic confirms significance of the model to test the hypotheses.

CONCLUSION

This study dealt with the relationship between features of companies with quality of financial reporting. The results showed a significant relationship between profitability and quality of financial reporting. In this regard, it can be said that increasing company’s profitability and ability to pay debts cause to meet expectations of capital market. Therefore, in such circumstances, managers use less discretionary accrual items that will ultimately improve quality of financial reporting. The results showed a significant relationship between liquidity and quality of financial reporting. One of causes to increase liquidity in companies can be increasing operating cash flow. Operating cash flow will be increased in companies by increasing profits of cash sales. So it can be said that the more cash in profits, the more improve quality of financial reporting.

The results showed a significant relationship between rate of sales growth and quality of financial reporting. Increasing sales will improve profitability of company and as previously mentioned, increasing profitability can be a sign of growing trend of companies.

Finally, it is recommended to users of the results that we examined set of variables including features of company. There were identified variables by significant positive relationship with quality of financial reporting and to use the variables in investment decisions. For example, leverage ratio has a significant relationship with quality of financial reporting. It is better that companies’ liquidity, cash and profitability are considered when deciding. Companies’ profitability process over time with amount of operating cash and rate of sales growth should also be considered.
REFERENCES


