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CONFERINȚA INTERNAȚIONALĂ „PERSPECTIVE ÎN CONTABILITATE ȘI AUDIT”, EDIȚIA II, 16-18 OCTOMBRIE2014

Departamentul Contabilitate și Audit din cadrul Universității de Vest din Timișoara, Facultatea de Economie și de Administrare a Afacerilor a organizat, în perioada 16-18 octombrie a.c. **Conferința Internațională „Perspective în contabilitate și audit”.**

Conferința a fost organizată în parteneriat cu Asociația Internațională a Experților Contabili Autorizați (ACCA), Corpul Experților Contabili și a Contabililor Autorizați din România (CECCAR), Camera Auditorilor Financiari din România (CAFR) și a fost susținută de mari cabinete de audit și consultanță în contabilitate KPMG, Ernst & Young, PriceWaterhouse Coopers, ABA, de companii prezente în mediul de afaceri, precum Bosch, Quasar etc.

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Conferința s-a bucurat deja de un deosebit interes și de o largă participare națională și internațională creând cadrul propice unor dezbateri științifice relevante privind provocările pe care noile tendințe și reglementări în domeniul financiar-contabil și cel al auditului le ridică în fața oricărui economist, profesionist și cercetător în domeniul larg al științelor economice.

Sesiunea plenara a avut trei speakeri deosebiți, cu prelegeri foarte interesante, originale și de actualitate: profesor univ. dr. Tudor Prisecaru, ministru secretar de stat în Ministerul Educației Naționale, Andreia Stanciu, director ACCA pentru Europea de Sud-Est, profesor univ. dr. Sylvie Heroux, Universitatea din Montreal (Canada). De altfel este pentru prima dată când la Facultatea de Economie și de Administrare a Afacerilor din Timișoara conferențiază, pe domeniul contabilitate, un cercetător de peste Ocean.

Au fost înscrise un număr de 48 lucrări științifice la cele 14 secțiuni ale Conferinței: Raportare financiară, Contabilitate și fiscalitate, Guvernanță corporativă, Audit, Profesia contabilă, Contabilitate în sectorul public, Educație și profesie contabilă, Provocări contabile. La lucrările conferinței și-au dat concursul doctoranzi, profesioniști în domeniul auditului și contabilității, cercetători consacrați din învățământul superior economic românesc și din 13 țări: Canada, Anglia, Franța, Slovenia, Austria, Spania, Grecia, Portugalia, Cipru, Ungaria, Scoția, Croația, Moldova.

Conferinta a avut mai multe secțiuni speciale dedicate tinerilor doctoranzi din domeniul contabilitate, iar un juriu internațional a oferit două premii celor mai bune lucrări apreciate pe baza unor criterii obiective utilizate în cercetarea științifică internațională.

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„Şcoala de contabilitate a Universității de Vest din Timişoara demonstrează că este la nivelul preocupărilor naționale și internaționale în domeniu prin organizarea și promovarea unei conferințe pe teme de actualitate. Această a doua ediție a scos la rampă și pe tinerii cercetători ai domeniului contabilitate care au participat proactiv la lucrările conferinței, în ambele zile, dar și la programul de socializare. Doresc să mulțumesc atât participanților și invitaților care au avut trei zile pline, dar și celor care ne-au susținut moral, material și financiar și cu siguranță roadele se vor vede de o manieră directă" a menţionat preşedintele Comitetului de Organizare al Conferinței, Conferențiar Universitar Dr. Ovidiu-Constantin Bunget, Directorul Departamentului de Contabilitate și Audit

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MEASUREMENT OF FINANCIAL REPORTING QUALITY BASED ON IFRS CONCEPTUAL FRAMEWORK'S FUNDAMENTAL QUALITATIVE CHARACTERISTICS

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Abstract

The IASB creates the standards and the conceptual framework in an attempt to create higher quality financial statements. Through this article, the extent to which this objective has been achieved is examined. An important characteristic of this research is the fact that the quality of financial statements is examined in light of the Conceptual Framework. Specifically, the two fundamental qualitative characteristics - relevance and faithful representation (reliability) - set by the IAS Committee through the Conceptual Framework are examined. Additionally, this article highlights the conflict between the existing methods for measuring reliability and the faithful representation, as defined by the Conceptual Framework. The degree of relevance and reliability is measured by the usage of four alternative regression models. The sample of this research consists of listed companies of fifteen European countries that have adopted IFRS mandatorily and the time horizon that is investigated is 10 years, from 2000 until 2009. Specifically, the period between 2000 and 2004 is defined as the period before the adoption, while the period between 2005 and 2009 is defined as the period after the adoption. Generally, the findings that are obtained support an increase in relevance, while the reliability seems to be unchanged.

Keyword: Adoption of IFRS; Financial Reporting quality; Conceptual Framework; Qualitative Characteristics; Relevance; Faithfull Representation (Reliability).

JEL Classification: M41, M48

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I. Introduction

Following the decision taken in March 2002, the European Parliament decided to adopt the International Accounting Standards (IAS). Specifically, since 2005 all listed companies are required to prepare and present the consolidated financial statements in accordance with the International Financial Reporting Standards (IFRS). The decision regarding the implementation of the IFRS constitutes a significant and unprecedented change concerning the way financial statements are prepared and presented.

The ultimate purpose of the Committee of the International Accounting Standards Board (IASB) is to create high quality standards in order to create quality financial statements. To achieve this objective, the Commission establishes those standards that lead to the increase in the degree of relevance, faithful representation, comparability, timeliness, verifiability and understandability in financial statements. The Commission stresses that the financial statements must reflect the specific characteristics, as defined by the Conceptual Framework, so that the information which is provided is useful.

In particular, the qualitative characteristics that are found in the Conceptual Framework are divided into fundamental and enhancing. The two fundamental characteristics are the relevance and faithful representation (i.e. an alternative definition of reliability), and the enhancing are the comparability, timeliness, understandability and verifiability. The main difference between the fundamental and enhancing characteristics is that the enhancing characteristics cannot single-handedly generate useful information.

As already mentioned, the IFRS creates the standards as well as the Conceptual Framework, essentially aiming in producing higher quality financial statements. The critical question that arises is whether this goal has been achieved; that is, whether the financial statements following the IASB adoption are in fact, of higher quality.

An important characteristic and a significant contribution of this research is the fact that the quality measurement methodology used varies greatly from other existing methodologies that are identified in the existing literature. Specifically, this research examines the quality of financial statements, as defined by the Conceptual Framework and the findings are expected to show whether the Commission actually achieved its initial objectives, enhancing the quality and usefulness of financial statements.

Based on existing literature, the quality is measured using different methods or, a combination of them, such as, by calculating discretionary accruals, conservatism,

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relevance and predictability of earnings. However, in some occasions a conflict between these methods and the degree of quality as defined by the Conceptual Framework can emerge. A typical example that highlights that conflict, concerns the measure of reliability. Literature supports that the degree of reliability is measured by the ability of current earnings to predict future earnings (Bandyopadhyay et al., 2010, Kirschenheiter 1997, Richardson et al., 2005). The problem arising out of this way of measurement is that it contradicts with the definition of reliability/faithful representation as defined by the Conceptual Framework. This conflict can be readily understood through the following example. Suppose a company makes use of fair value as the valuation method, which essentially introduces variability in the results by reducing their predictability. Given that the fair value is reflected without error, presenting faithfully the economic reality, the level of faithful representation based on the definition derived from the Conceptual Framework is very high, whereas based on the measure of predictability in contrast, is very low (Riedl, 2010).

Another element that highlights the aforementioned conflict relates to the measure of conservatism. The high degree of conservatism in the literature (Anwer et al., 2013, Ball et al., 2000, Ball and Shivakumar 2005, Barth et al., 2008, Chen, et al., 2010) is presented as an indication of high quality financial statements. In contrast, this feature is not considered desirable by the new Conceptual Framework - since it conflicts with the feature of neutrality - and therefore, it is not included in it.

The findings of this research constitute a useful tool both for the Commission as well as for users of financial statements. On the one hand, the Commission will be able to know the degree of achievement of the objectives set initially and to take the necessary actions/improvements wherever is deemed appropriate. On the other hand, users who know about the relevance and reliability - with respect to the financial statements - are more equipped to make favorable decisions for their part.

II. Conceptual Framework

The conceptual framework of IAS essentially defines the general principles which should characterize the process of preparing and presenting financial statements. In no case does it have the power of a standard and the basic purpose of its creation is to help and guide the IASB to develop or review existing and future IAS. Furthermore, it directs those preparing the financial statements to correctly apply the standards and is an additional tool for handling accounting issues not covered by existing standards. At this

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stage it should be noted that if an existing standard conflicts with the conceptual framework, then the standard shall prevail. Finally, it helps auditors and users to understand whether the financial statements and the information provided is consistent with IAS.

The qualitative characteristics are divided into fundamental and enhancing. The fundamental features are designed to separate the information provided to users in the following parts: useful information or non-useful and/or misleading information. The two fundamental characteristics include relevance and faithful representation. The conceptual framework highlights (paragraph 17) that in order for the information to be useful, it must be characterized by both of the aforementioned characteristics, i.e. relevance and faithful representation.

The first fundamental characteristic is relevance, meaning that financial statements can and influence the decisions of users. In other words, they can be used as predictive values and/or confirmatory values. In addition, relevance may be affected by whether a piece of information is essential, i.e. whether its omission or incorrect portrayal affects the economic decisions taken by users.

The second fundamental feature is the faithful representation/reliability of financial statements. The conceptual framework focuses on five specific features which should be reflected on the financial statements so as to be considered reliable. First, financial statements should present faithfully the economic events; secondly, they should not be the product of any prejudice whatsoever, that is to be neutral; third, should present the economic substance of economic events unconstrained by legal aspects; fourth, decisions taken by the management regarding uncertain events which require the exercise of judgment must be taken with caution and finally, the financial statements ought to be complete.

In addition, the IASB defines four enhancing qualitative characteristics considered complementary to the fundamental characteristics. The main difference with the fundamental characteristics is that if the financial information is not characterized by the fundamental characteristics, then the enhancing characteristics alone cannot generate useful information to users. Specifically, the enhancing characteristics are comparability, timeliness, understandability and verifiability.

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III. Literature Review

III.1. Relevance and Adoption of IAS

Extensive literature has dealt with the subject of relevance of financial statements. At this point, it is noteworthy that the first researchers who wrote about it were Ball and Brown, in 1968. They examined the relationship between performance and accounting profit, stimulating future research.

Over the past few years and following the adoption of IAS, researchers have extended the literature concerning relevance, assessing the relevance of financial statements prepared in accordance with national accounting standards and those prepared in accordance with IAS. This research can be divided into two major parts; one focusing on the studies using as sample the firms adopting IAS voluntarily and those that use as sample companies whose adoption of the standards in question is mandatory.

In the first category several research articles are identified. More specifically, Hung and Subramanyam (2007) examine 80 German companies. Comparing the financial statements prepared under IAS/IFRS as those drawn up by the German standards and using the relative degree of relevance, do not detect any change in the relevance of earnings and of the book value of equity. Furthermore, measuring relevance using the incremental approach, they found that the adjustments to the balance sheet data generated due to the adoption of IAS were relevant, while adjustments to the earnings were not. In contrast, Bartov et al. (2005) and Jermakowicz et al. (2007), identify an increase in the degree of relevance of earnings of companies adopting voluntarily the IAS. Barth et al. (2008), using a larger sample than previous research, by examining 319 companies from 21 countries that voluntarily adopt IFRS identify, inter alia, that the degree of relevance of firms adopting IAS is higher.

More recent studies dealing with the second category examine the change in relevance of the financial statements of those companies that mandatorily adopt IAS. Horton and Serafeim (2007) study the relevance of the financial statements of companies in the United Kingdom, France, Italy and Spain, using accounting adjustments arising from the reconciliation statements. Their findings suggest that adjustments in the earnings increase relevance in the UK, France and Italy, while this is not the case in Spain. The same researchers in 2010 examine relevance once more only this time, exclusively for the UK. Their findings again suggest that the adjustments regarding the earnings have a positive contribution to the degree of relevance. In contrast, adjustments in the book value of equity have no positive contribution to the degree of relevance since the calculation of the book value of equity through both IAS and by the standards applied in the UK is similar (Horton and Serafeim, 2010). Similar results in respect to the UK are reached in 2008 by Capkun et al. The same researchers in their article incorporate eight other European countries besides the UK, identifying once again that adjustments regarding the earnings contribute to relevance whilst this does not apply to adjustments in the book value of equity. Christensen et al. in 2009, also identify an increase in relevance of the earnings regarding the case of the UK. The findings of Wang et al. (2008) concerning the Australian companies as well as 14 European countries follow the same pattern, in respect to the relevance of the earnings.

Finally, the part of the literature that utilizes two independent samples - financial statements before and after adoption - in order to detect the change of relevance of the financial statements for mandatorily adopters – is extremely limited. Chalmers et al. (2009) identify through this methodology that the earnings (book value of equity) of Australian businesses that adopt mandatory IFRS for the period 2006-2007 reflect higher (the same) degree of relevance in relation to the degree of relevance which reflected by the Australian businesses using the Australian standards during the period 1990-2004.

III.2. Reliability/Faithfull representation and Adoption of IAS

Although IAS gives equal emphasis on the feature of relevance and reliability through their conceptual framework, the same does not apply as far as the literature is concerned. On one side, a significant proportion of the literature has dealt extensively with the feature of relevance and how this is reflected in the financial statements. In antithesis, the emphasis of the characteristic of reliability is very limited (Richardson et al. 2005).

The vast majority of the literature examines the feature of reliability of accruals through the estimation of discretionary (DA) and non-discretionary accruals (NDA). Several researchers have created models for measuring the degree of reliability using this methodology (Healy 1985, De Angelo 1986, Jones 1991, Dechow and Sloan 1991, Dechow et al. 1995), which are then used as tools for further research. Moreover, the concept of reliability of accruals has been identified with the concept of quality of accruals directly related to the literature that deals with the quality of earnings.

Escaping from the basic idea of the above researchers, recently some researchers identify the quality of accruals and earnings by measuring the amount of error that arises

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from the relation between accruals and cash flows (Dechow and Dichev 2002, McNichols 2002).

In 2007, White, escaping heavily from the methodology of Dechow and Dichev (2002) and McNichols (2002), creates a new model that examines the extent to which the accruals at time t are converted into cash flow in year t +1. In comparison to the previous models, significant differences lie in that the calculation of accruals is not based on their changes, but on the closing balances of the accounts. Moreover and in antithesis with Dechow and Dichev (2002) and McNichols (2002), the model does not have as independent variables the overall operating cash flows, which acts as the cause for the introduction of error.

Beyond the research dealing with the reliability of accruals, only a very small part of the literature deals with the reliability of specific accounting items or financial statements as a whole.

Cotter and Richardson (2002), in order to identify the reliability of asset revaluations, compare the valuation of intangible assets arising from independent appraisers, with estimates arising from the board of the company. The findings identified that the valuations of plant and equipment that have been made by independent appraisers, are more reliable. For other non-current assets, no difference in the degree of reliability of valuations has been detected.

Cotter and Richardson identify the degree of reliability by examining the write-downs of an upward revaluation that took place in the past. They claim that the greater the reversal the lower the reliability, as a great reversal implies that there was greater error in the initial revaluation.

In 2007, Lanito detects the degree of reliability of IAS in Finnish companies through questionnaires that target business managers and auditors of financial statements. The findings resulting from the responses, both for managers and auditors, recognize as reliable the information provided by several standards whilst the findings regarding those standards requiring the exercise of judgment, are characterized as neutral.

Richardson et al. (2005) and Bandyopadhyay et al. (2010), measure the degree of reliability through the ability of current earnings to predict the earnings of the following period. This is based on the argument that the error arising from accruals is incorporated to the process of calculating the earnings, consequently weakening the relationship between successive earnings. In other words, the larger the error in the current earnings is, the lower the correlation to future earnings, leading to a lower degree of persistence/predictive power. An important problem that arises is that this way of measuring reliability is not consistent with the definition of reliability, as it emerges from the conceptual framework of IAS. It is alleged that this method may lead to conflicting findings concerning the degree of reliability, especially when the revaluation model is used. In particular, it is argued that the use of fair value introduces additional variation in earrings while reducing their predictive ability. Therefore, based on the empirical model of Richardson et al. (2005), the degree of reliability would be characterized as low whilst by the definition derived from the conceptual framework, the reliability is high (as long as the fair values are portrayed without error, presenting the faithfully the economic reality).

Finally, the findings associated with the reliability and adoption of IAS are identified in 2005 from Van Tendeloo and Vanstraelen, discovering while using the model of Jones (1991), that the financial statements of German firms that voluntarily adopt IAS are characterized by higher degree of DA, compared with companies that do not adopt IAS. In addition, Chen, Tang et al. (2010) who examine 15 European countries and apply inter alia the modified model of Jones and Kothari et al., discover opposite results as compared with the findings of the Van Tendeloo and Vanstraelen (2005). Particularly, they find that the degree of DA is lower in firms adopting IAS, which supports the increase in the quality of their financial statements. In addition, the same researchers examine the quality of accruals through the model proposed in 2002 by the Dechow and Dichev, identifying a reduction in standard deviation of the residuals of the model, which again supports the rise in quality.

IV. Hypothesis development

IV.1. Relevance of Financial Statements and IAS Adoption

Financial statements may be characterized by a high degree of relevance either when used to predict future events or when they confirm predictions and actions of the past.

Accounting regimes of several countries that adopted IFRS were stakeholder-oriented, with the main purpose to inform stakeholders (state, creditors, banks, etc.). As a natural consequence, the financial statements were prepared with the basic aim of providing information mainly to creditors and the state, rather than to the shareholders/investors, thereby reducing the degree of relevance of financial statements for shareholders. Various accounting options that were identified prior to the adoption of IAS and reinforce this case were the use of historical values, which in many cases had nothing to do with the current economic prices. Moreover, the excessive emphasis on some accounting principles, such as the matching concept and principle of prudence, had as a consequence the restriction of relevance in the financial statements, as these characteristics impeded the immediate recognition of the economic events in the financial statements.

In contrast, the purpose of the Committee of the International Accounting Standards Board has been the creation of standards, mainly oriented to the needs of shareholders; thus, giving them, through the financial statements, more relevant information. The use of fair value and less frequent use of historical cost, the weakening of the principle of the matching concept and the reduction of the degree of conservatism resulted, first, the accounting amounts reflected in the financial statements to converge to the current economic prices and secondly, the financial information to be integrated in a more timely manner to financial statements. Both of these features lead to an increase in the degree of relevance, since most financial statements reflect more directly the current economic events which help investors in making timely investment decisions.

Finally, by increasing the degree of comparability between the financial statements at both national and international level, investors are able to identify more easily investment opportunities arising from the comparison of the financial statements of two or more companies in the same industry. The degree of comparability at the international level is therefore enhanced, as most financial statements are based on common accounting standards. Indeed, prior to the adoption of IAS, because of the differing accounting systems of each country, this comparison was more difficult to achieve and at a higher cost as the users had to make the necessary adjustments between different accounting systems. Alternatively, after the adoption of IAS, comparison is achieved a lot easier and at a lower cost. In addition, comparability at the national level is also enhanced, since the use of fair value as the valuation method facilitates users to perform better comparisons. Business items that are measured at fair value are easier to compare, given that all are calculated for the current period (i.e. there is a common basis for comparison for all businesses which is considered as a basis). Instead, the historical cost of the assets of each company is based on a different point in time, thereby, resulting a priori in the incorrect comparison. In conclusion, increasing the degree of comparability both at national and international level creates an additional source of information to users, helping them in making investment decisions and increasing the usefulness of financial statements.

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In summary, following the adoption of IAS investors will be able to take timely and with greater ease more relevant information from the financial statements, which will aid them make better investment decisions. The hypothesis which arises is the following:

Hypothesis 1: The relevance (for shareholders/investors) of the financial statements of firms adopting IAS is greater for the period following the adoption of IAS as compared with the period before the adoption.

IV.1. Adoption of IAS and the degree of Faithfull representation/ Reliability of Financial Statements

Based on the definition of faithful representation/reliability as defined by the conceptual framework, the financial statements are said to be reliable when they do not contain any material error or bias and reliably reflect the economic events that they must present.

The purpose of the IAS Committee was the creation and provision, especially to investors, of augmented levels of relevance in the financial statements. Given the interaction between the characteristics of relevance and reliability, the increase of relevance will be attained by increasing the reliability of financial statements. To achieve this objective, the IASB has taken the following actions: First, reduction of alternative accounting methods (e.g. abolition of the LIFO method), which aims to reduce the degree of manipulation of results and thus increasing their reliability. Second, give focus on the economic substance of events, giving in many cases the option to managements to choose the accounting treatment (e.g. introduction of fair value as the valuation method) resulting to the better reflection of economic reality in the financial statements.

In addition, the detailed presentation of the principles relating to valuation, recognition and publication of the financial statements, suggests that the degree of manipulation by the management is reduced and at the same time a rise in terms of completeness is observed.

Additionally, with the adoption of IAS and the increase of the degree of comparability, especially at international level, investors are able to compare at a lower cost the financial statements, identifying omissions and/or errors in accounting statements easier. This leads both, managements and audit firms that audit the financial statements, to be more careful in the drafting and auditing of accounts, resulting in more reliable financial statements.

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On the other hand, in some cases, the use of fair value and the exercise of judgment by the management may result in the rise of the degree of manipulation. Moreover, the difficulty of calculating the fair value can introduce additional estimation error. These elements can cause loss of reliability, but are not considered likely to lead to a reduction in the reliability of the financial statements in the period following the adoption of IAS.

If one relies on the definition of reliability, developed in the first paragraph of this section, it can be drawn that before the adoption of IFRS the financial statements were governed by a low degree of reliability, since due to the use of historical cost the accounting data did not adequately describe the economic reality, because the book values of a firm deviate significantly from the economic values. The deviation from the economic reality - an indication of low-level reliability - resulting from the use of historical cost is expected to be greater than the deviation caused by the use of fair value, upon adoption (which as mentioned above, in some cases can be manipulated or can be inaccurate).

As a final point, the possibility that the elements that seem to reduce the reliability of financial statements - such as those developed in the previous paragraph - seems unlikely to prevail and lead to the reduction of the degree of reliability. This assumption combined with the actions taken by the International Accounting Standards Board to increase the reliability, lead to the following hypothesis:

Hypothesis 2: The faithful representation/reliability of the financial statements of firms adopting IAS is higher during the period following the adoption of IAS in relation to the period before the adoption.

V. Methodology

V.1. Relevance and Adoption of IAS

The relevance of financial statements is measured using two alternative methods. The first method examines the relevance through the linear model that has as independent variables the earnings and the book value of equity, with the share price six months after the end of the fiscal year as a dependent. The second method examines the relevance through the linear model that has as independent variables the total assets and total liabilities and the share price six months after the end of the fiscal year as the dependent.

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V.1.1. Measuring Relevance - First Method

The first method for measuring the relevance examines the relationship between accounting and market data. Specifically, the simultaneous relationship between both, the market price of a share at time t+6 months and also, the accounting results along with the book value of equity at time t, is examined (Francis and Schipper 1999, Barth et al., 2008, Kim and Kross, 2005). Furthermore, following a similar methodology with Bartov et al. 2005, (incremental approach), the dummy variable Post is introduced in the model, in an attempt to identify the changes (resulting due to the transition of countries in IAS) of the two independent variables of the model. The model developed is the following:

$$P_{it+6} = a_0 + a_1 Post + a_2 Bvps_{it} + a_3 Eps(1)_{it} + a_4\, Post{*}Bvps_{it} + a_5\, Post{*}Eps_{it} + u_{it+6} \quad (1)$$

P_{it+6} = Market share price at time t +6 months,
$Bvps_{it}$ = Book value of equity per share,
Eps (1) $_{it}$ = Income (before extraordinary items) per share,
Post = Dummy - variable equals to 1 for the period after the adoption of IAS and to 0 for the period prior.
U_{it+6} = residuals

Essentially, the ability of earnings and the book value of equity to explain future stock prices are identified using the model (1). The higher this ability is, the higher the degree of relevance of specific accounting data is, since users are able to make better investment decisions. Moreover, the change in relevance of the financial statements prepared according to IFRS (period after the adoption of IFRS) is revealed through the Post dummy variable. Specifically, for the period after the adoption, the coefficient of the book value of equity is equal to a2 plus a4 and the coefficient of earnings is equal to a3 plus a5. Thus, if the coefficients a4 and a5 are positive (negative) and statistically significant, it implies that the relevance of the book value of equity and earnings respectively, are larger (smaller) in the period following the adoption.

Finally, the relative approach is also used to detect the change of relevance. Specifically, the R2 of regression (2) is identified for each period separately (before and after adoption).

$$P_{it+6} = a_0 + a_1 Bvps_{it} + a_2\, Eps\,(1)_{it} + u_{it+6} \quad (2)$$

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If the coefficient of determination (R2), after the adoption of IAS, is higher (lower), it means that the explanatory ability of the two independent variables on future stock prices is higher (lower), indicating the increase (decrease) of the degree of relevance of book value of equity and earnings. The statistical significance of the difference between the two R2 is examined through a test used by Van der Meulen et al. in 2007, which was based on the analysis of Crammer (1987) (appendix1).

V.1.2. Measuring Relevance - Second Method

The second method for measuring relevance examines the relationship between balance sheet information and market data. The methodology that is being followed is similar to the previous one. In this case, the simultaneous relationship between the market price of one share at time t + 6 months and the total assets and total liabilities at time t, is examined (Francis, 1999). The variable Post is introduced again to identify differences between the periods ex antes and ex post the adoption. The model developed is as follows:

$$P_{it+6} = a_0 + a_1 Post + a_2 TA_{it} + a3\ TL_{it} + a_4\ Post*TA_{it} + a_5\ Post*TL_{it} + u_{it+6} \qquad (3)$$

P_{it+6} = Market share price at time t +6 months,
TA_{it} = Total assets per share,
TL_{it} = Total liabilities per share,
Post = Dummy-variable equals to 1 for the period after the adoption of IAS and to 0 for the period prior.
U_{it+6} = residuals

Through the model (3), the ability of the total assets and total liabilities to explain the future stock prices is revealed. As in the previous model, the higher that ability is, the higher the degree of relevance of specific accounting items. To detect the change of relevance between the two periods - before and after the adoption - variable Post is reentered. So, for the period after the adoption the coefficient of total assets is equal to a2 plus a4, while the coefficient of total liabilities equals a3 plus a5. Unlike the first model, the signs of the coefficients are not expected to be all positive. The fact that an increase in total assets is expected to result in an increase in the stock price, while an increase in total liabilities is expected to reduce the stock price, results in the coefficient a2 to be expected positive, whereas the a3 to be expected negative. For this reason, in case of increase

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(decrease) of relevance of total liabilities upon adoption, a5 is expected to be negative (positive) and statistically significant. Conversely, when total assets are more (less) relevant after the adoption, a4 is predicted to be positive (negative) and statistically significant.

To detect the change of relevance (as in the first method), the relative approach is used interchangeably. Specifically, the R2 of regression (4) for each period separately (before and after adoption) is identified.

$$P_{it+6} = a_0 + a_1 TA_{it} + a_2 TL_{it} + u_{it+6} \qquad (4)$$

V.2. Reliability/Faithfull representation and Adoption of IAS

The reliability of the financial statements is measured by two alternative methods. The first method examines the degree of reliability through the linear model with cash flows from operating activities and accruals at time t acting as independent variables, while cash flows from operating activities in t + 1 are designated as the dependent variable. The second method examines the degree of reliability through the linear model that defines the following independent variables: 1) accruals (amounts recognized in the year t and which are disbursed to the next), 2) Cpcf, amounts recognized in the year t and disbursed in it and 3) deferrals (amounts relating to the fiscal year t+2 and disbursed to t +1) and the cash flows from operating activities in t +1 as the dependent variable.

V.2.1.. Measuring reliability - First Method

The first model used to measure the reliability has been developed by Kim and Kross (2005). Specifically, cash flows from operating activities and accruals at time t are set as the independent variables, whilst the cash flows from operating activities in t +1 as the dependent variable. The model which emerges is the following:

$$Cfo_{it+1} = a_0 + a_1 Cfo_{it} + a_2 Acc_{it} + u_{it+1} \qquad (5)$$

Cfo_{it+1} = Cash flows from operating activities in t + 1 / Total assets at t,
Cfo_{it} = Cash flows from operating activities in t / Total assets at t-1,
Acc_{it} = DWC - DEP,
DEP = Depreciation / Total Assets at t-1,

DWC = change in net accounts Receivables / total assets at t-1, plus change in inventory / Total assets at t-1, plus change in other current assets / total assets at t-1, minus change in accounts payable / Total assets at t-1, minus change in taxes payable / total assets at t-1, minus change in other current liabilities / Total assets at t-1, minus change in deferred taxes / Total assets at t-1.

U_{it+1} = residuals

Reliability is defined as the ability of the two independent variables to explain the cash flows from operating activities in t +1. This ability is identified by the coefficient of determination of the model (R2). In other words, the identification of higher R2 indicates a higher degree of reliability of the financial statements and, vice versa. The comparison of reliability between the two periods - before and after the adoption - is performed by comparing the R2 of two independent samples. Once more, the statistical significance of the difference between the two R2 is examined through the test used by Van der Meulen et al, in 2007.

V.2.2. Measuring reliability - Second Method

The second model used to measure reliability is based on the model developed by White, in 2007. Two important properties of the model is that the calculation of accruals is not based on changes in the accounting items ('traditional' approach), as older models (Dechow and Dichev, 2002, McNichols, 2002, Kim and Kross, 2005 etc.), but on their closing balances. Furthermore, a distinction between accruals and deferrals is made, escaping from the hitherto definition of accruals that integrated the cumulative accruals and deferrals.

The underlying logic of the model is to isolate the amounts recognized in the year t and which are disbursed to the next (t +1) (payable/accruals), the amounts recognized in the year t +1 and disbursed to it as well as the amounts disbursed in fiscal year t +1 and related to upcoming year (prepaid/deferrals). Finally, White (2007) examines the ability of these three variables to explain the cash flows at t +1. A basic assumption of the model is the hypothesis that short-term assets and liabilities are recovered or settled, within twelve months.

The higher the capacity of the three independent variables in explaining the dependent variable is, the higher the degree of reliability of the financial statements. In other words, when the accruals (payable/accruals at time t and prepaid/deferrals at time

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t+1) explain the operating cash flows at time t+1, then the management estimates relating to accruals can be regarded as reliable. Finally, White (2007) argues that the introduction of the independent variable Cpcfit+1 introduces systematic measurement error in the regression (White, 2007: 18). Hence, he uses a proxy variable; the Cpcfit. The model which emerges is the following:

$$Cfo_{it+1} = a_0 + a_1Accr_{it} + a_2Cpcf_{it} + a_3Def_{it+1} + u_{it+1} \quad (6)$$

Cfo_{it+1} = Cash flows from operating activities in t + 1 / Total assets at t,
$Accr_{it}$ = Net accounts receivables / Total assets at t-1, minus other current liabilities / Total assets at t-1, minus inventory accruals / Total assets at t-1,
$Cpcf_{it}$ = operating income before depreciation at time t minus Accr it plus Def it-1.
Def_{it+1} = other current assets / Total assets at t, plus inventory deferrals / Total assets at t,
U_{it+1} = residuals

Once again, the explanatory ability of the independent variables is measured by the coefficient of determination of the model (R2). The higher the R2 is, the more reliable the financial statements and, vice versa. As in the previous model, the comparison of reliability between the two periods - before and after the adoption - is performed by comparing the R2 of two independent samples.

VI. Sample

The sample of this study consists of listed companies of 15 European countries, which according to the classification published by the FTSE Group in September 2009 (FTSE, Country Classification, 2009) are characterized as developed. The countries considered are: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden and the UK.

The time period under study for this research is 10 years, and consists of the period prior (2000-2004) and the period after (2005-2009) the adoption of IAS. Given that the effects of IFRS on the financial statements of companies that are mandatory IAS adopters are the ones examined, firms which are either voluntary adopters of IAS, or whether they adopt them at a time after 2005 (as listed on AIM London Stock Exchange - alternative investment market) are excluded from the sample. In other words, any firms

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whose first publication of their financial statements under IAS was held a year other than 2005 are crossed out from the sample.

The data for the sample was provided by DataStream database. In addition, other than the aforementioned exceptions, firms in the financial sector are also excluded (so that the findings can be directly compared with previous research), since the exclusion of financial firms from samples of previous research that are related is almost ubiquitous. Additionally, according to the existing literature, companies with negative book value of capital are excluded. Among others, Collins et al (1997) and Collins et al. (1999) and Brown et al. (1999) argue that the samples used for the measurement of relevance should incorporate only positive observations of book value of equity. In addition, 2% of the extreme values is deleted. The process of the creation of the final samples, as discussed in the previous paragraphs, is summarized in Table 1.

Table 1 – Sample selection for IFRS mandatory adopters

	(N) 2000 - 2004	(N) 2005 - 2009	(N) 2000 - 2009
Original sample	26876	23047	49923
Minus:			
Observations for companies / fiscal year different from 1/1-31/12	7495	6501	13996
Observations for companies in the financial sector	1615	1459	3074
Observations for companies with negative book value of equity	581	572	1153
Voluntary adopters	7711	6686	14397
Data not available	437	449	886
Outliers (2%)	136	191	327
Final sample	8662	7428	16090

This sample is referred to relevance measure resulting from regression Pit +6 = a0 + a1Post + a2 Bvpsit + a3 Epsit + a4 Post * Bvpsit + a5 Post * Epsit. Observations arising from other models vary, depending on the unavailable data.

VII. Results

VII.1. Descriptive Statistics

In Table 2 the descriptive elements of the sample are presented. Specifically, it presents the descriptive elements of the 15 countries examined (cumulative). A detailed description of the variables used is presented in the table. It is observed that in the period following the adoption of IAS there is a statistically significant increase in both the averages, and the median book value of equity and earnings. In contrast, the average of total assets and total liabilities do not appear to differ between the two periods.

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Table 2 - Descriptive statistics

Variable / Model	2000-2004					2005-2009				
	Mean	Median	Q1	Q3	Sd	Mean	Median	Q1	Q3	Sd
Relevance 1										
Pt+6	15.43	4.49	1.58	12.80	43.36	19.63***	6.17***	2.00	17.6	50.12
Bvps t	10.61	2.46	0.93	7.20	50.83	12.60***	3.26***	1.29	9.17	42.14
Eps(1) t	0.52	0.14	-0.04	0.68	5.49	1.12***	0.28***	0.016	1.1	4.65
Relevance 2										
Pt+6	14.14	4.55	1.62	12.90	32.52	17.32***	6.10***	2.00	17.30	35.66
TA t	35.46	8.48	2.51	27.09	101.15	33.67	9.24***	3.46	26.94	89.89
TL t	21.66	4.49	1.07	16.17	65.65	20.58	5.01***	1.75	15.92	61.42
Reliability 1										
Cfot+1	0,07	0,08	0,03	0,12	0,15	0,07	0.07***	0,03	0,12	0,11
Accr t	0,08	0,08	-0,01	0,18	0,2	0,08	0,08	-0,01	0,18	0,17
Cpcf t	0,07	0,06	-0,05	0,17	0,27	0.08***	0.08***	-0,05	0,19	0,22
Def t+1	0,07	0,03	0,01	0,1	0,11	0.06**	0.02***	0,00	0,1	0,1
Reliability 2										
Cfot+1	0,09	0,09	0,05	0,13	0,09	0.08***	0.08***	0,04	0,12	0,08
Cfo t	0,08	0,08	0,05	0,12	0,09	0.09***	0.09***	0,05	0,13	0,08
Acc	-0,05	-0,06	-0,09	-0,02	0,09	-0.04***	0.03***	-0,07	0,00	0,08

The model Relevance 1 refers to the regression : Pit +6months = a0 + a1Bvpsit + a2Eps (1) it + a3Post * Bvpsit + a4Post * Eps (1) it, the model Relevance 2 refers to the regression : Pit +6months = a0 + a1TAit + a2TLit + a3 Post * TAit + a4 Post * TLit, the model Reliability 1 refers to the regression : Cfoit +1year = a0 + a1Accrit + a2Cpcfit + a3Defit +1year, and model Reliability 2 refers to the regression : Cfoit +1year = a0 + a1Cfoit + a2Accit. Variables : Pit +6 months = Market share price at time t +6, Bvps it = Book value of equity per share , Eps (1) it = Income (before extraordinary items) per share , Post = dummy-variable that takes the value 1 for the period after the adoption of IAS and the value 0 for the period prior , TA it = Total assets per share , TL it = Total liabilities per share , Cfo it +1 = Cash flows from operating activities in t + 1 / Total assets at t, Cfo it = Cash flows from operating activities in t / Total assets at t-1, Accr it = Net accounts receivables / Total assets at t-1, minus other current liabilities / Total assets at t-1, minus inventory accruals / Total assets at t-1, Def it +1 = Other current assets / Total assets at t, plus inventory deferrals / Total assets at t, Cpcf it = operating income before depreciation at time t minus Accr it plus Def it-1, Accit = DWC - DEP, DEP = Depreciation / Total Assets at t-1, DWC = change in net accounts Receivables / total assets at t-1, plus change in inventory / Total assets at t-1, plus change in other current assets / total assets at t-1, minus change in accounts payable / Total assets at t-1, minus change in taxes payable / total assets at t-1, minus change in other current liabilities / Total assets at t-1, minus change in deferred taxes / Total assets at t-1, *** = 1% statistically significant , ** = 5% statistically significant , * = 10% statistically significant, T-test and Wilcoxon rank sum test have been used to test for differences means and median, respectively.

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VII.2. Empirical Findings

VII.2.1. Degree of Relevance and Adoption of IAS

According to the first hypothesis, the degree of relevance of the financial statements is expected to be higher during the period following the adoption of IAS, as compared with the period before.

Table 3 illustrates the degree of relevance of earnings and the book value of equity, with respect to the stock price six months after the end of the year. The degree of relevance is tested both through the incremental approach as well as the relative approach.

The earnings seem to be more relevant in the period after the adoption since the coefficient a5 is positive (2.27) and statistically significant at the 1% significance level. Regarding the variable of the book value of equity and the degree of relevance, the findings (Horton and Serafeim (2010) and Capkun et al. (2008) identify similar results regarding the degree of relevance regarding equities in the UK. Specifically, a change in equity relevance is not detected) that are identified are not statistically significant, but remain in the same direction.

The results obtained from the relative approach are consistent with the findings obtained through the incremental approach, again indicating increase of relevance. Specifically, the coefficient of determination is higher for the period after the adoption at a significance level of 5%. The findings suggest that the explanatory ability of the two independent variables on future stock prices (t+6) is higher in the period after the adoption of IAS, suggesting an increase in the degree of relevance of book value of equity and earnings.

Table 3 - Relevance Model 1

	Incremental Approach $P_{it+6} = a_0 + a_1Post + a_2Bvps_{it} + a_3Eps(1)_{it} + a_4 Post{*}Bvps_{it} + a_5 Post{*}Eps(1)_{it} + u_{it+6}$ (1)							Relative Approach $P_{it+6} = a_0 + a_1Bvps_{it} + a_2Eps(1)_{it} + u_{it+6}$ (2)		
	a_0	a_1	a_2	a_3	a_4	a_5	2000-2009 Ad.R^2	2000-2004 Ad.R^2	2005-2009 Ad.R^2	Difference Ad.R^2
All countries	3.81***	-2.98*	0.33**	1.82***	0.22	2.27***	55%	52%	67%	15%**

Variables: Pit +6 = Market share price at time t +6 months, Bvps it = Book value of equity per share, Eps (1) it = Income (before extraordinary items) per share, Post = Dummy - variable equals to 1 for the period after the adoption of IAS and to 0 for the period prior. The technique bootstrapping (Van der Meulen et. al 2007 and Crammer 1986) is used to control the statistical significance of differences in R^2. *** = 1% statistical significance, ** = 5% statistically significant, * = 10% statistically significant.

Table 4 illustrates the degree of relevance of balance sheet items. More specifically, it examines the relevance of total assets and total liabilities with respect to the stock price six months after the end of the year. The degree of relevance is tested once again through both, the incremental approach and relative approach. At a significance level of 1% the degree of relevance of both total assets and total liabilities increased in the period after the adoption. In more detail, the coefficient a4 which reflects the change in the degree of relevance of the total assets is equal to 0.35 and coefficient a5, which reflects the change of relevance of all liabilities, is equal to -0.43.

At the same time, the results obtained from the relative approach (Table 4, regression 4) indicate a statistically significant increase in the coefficient of determination (the period following the adoption of IAS) at 1%. The findings suggest that the explanatory ability of the two independent variables on future stock prices (t+6) is higher in the period after the adoption of IAS, suggesting an increase in the degree of relevance of total assets and total liabilities.

Table 4 - Relevance Model 2

	Incremental Approach $P_{it+6} = a_0 + a_1Post + a_2TA_{it} + a3\ TL_{it} + a_4\ Post*TA_{it} + a_5\ Post*TL_{it} + u_{it+6}$ (3)							Relative Approach $P_{it+6} = a_0 + a_1TA_{it} + a_2TL_{it} + u_{it+6}$ (4)		
	a_0	a_1	a_2	a_3	a_4	a_5	2000-2009 Ad.R^2	2000-2004 Ad.R^2	2005-2009 Ad.R^2	Difference Ad.R^2
All countries	2.59***	0.45	0.29***	-0.22**	0.35***	-0.43***	44%	33%	46%	13%***

Variables: Pit +6 = Market share price at time t +6 months, TA it = Total assets per share, TL it = Total liabilities per share, Post = Dummy - variable equals to 1 for the period after the adoption of IAS and to 0 for the period prior. The technique bootstrapping (Van der Meulen et. al 2007 and Crammer 1986) is used to control the statistical significance of differences in R^2. *** = 1% statistical significance, ** = 5% statistically significant, * = 10% statistically significant.

VII.2.2. Adoption of IAS and the degree of Reliability of financial statements

According to the second hypothesis, reliability of financial statements is expected to increase in the period following the adoption of IAS. Tables 5 and 6 illustrate the findings on this matter.

The change of the degree of reliability is detected by the linear models 5 and 6 and more specifically, by examining the change of the coefficient of determination (R2). The results from both methods detect a marginal increase in the degree of reliability but are not statistically significant whatsoever. Specifically, the change of R2 regarding both, regression 5 and 6, shows a marginal non-significant increase in reliability at the rate of 3% and 2%, respectively (Table 5, 6).

Table 5 - Reliability Model 1

$$Cfo_{it+1} = a_0 + a_1\, Cfo_{it} + a_2 Acc_{it} + u_{it+1} \quad (5)$$

	a_0	a_1	a_2	Ad. R^2	Dif. R^2
All countries prior IAS	0.023369***	0,698654***	-0,093846***	51%	
All countries post IAS	0,014563***	0,679640***	-0.052264**	54%	+03%

Variables : Cfo it +1 = Cash flows from operating activities in t + 1 / Total assets at t, Cfo it = Cash flows from operating activities in t / Total assets at t-1, Accit = DWC - DEP, DEP = Depreciation / Total Assets at t-1, DWC = change in net accounts Receivables / total assets at t-1, plus change in inventory / Total assets at t-1, plus change in other current assets / total assets at t-1, minus change in accounts payable / Total assets at t-1, minus change in taxes payable / total assets at t-1, minus change in other current liabilities / Total assets at t-1, minus change in deferred taxes / Total assets at t-1. The technique bootstrapping (Van der Meulen et. al 2007 and Crammer 1986) is used to control the statistical significance of differences in R2. *** = 1% statistical significance, ** = 5% statistically significant, * = 10% statistically significant.

Table 6 - Reliability Model 2

$$Cfo_{it+1} = a_0 + a_1 Accr_{it} + a_2\, Cpcf_{it} + a3Def_{it+1} + u_{it+1} \quad (6)$$

	a_0	a_1	a_2	a_3	Ad. R^2	Dif. R^2
All countries prior IAS	0.025848***	0.442617***	0.459280***	-0.295475***	35%	
All countries post IAS	0.016293***	0.450523***	0.489532***	-0.333095***	37%	+02%

Variables : Cfo it +1 = Cash flows from operating activities in t + 1 / Total assets at t, Accr it = Net accounts receivables / Total assets at t-1, minus other current liabilities / Total assets at t-1, minus inventory accruals / Total assets at t-1, Def it +1 = Other current assets / Total assets at t, plus inventory deferrals / Total assets at t, Cpcf it = operating income before depreciation at time t minus Accr it plus Def it-1. The technique bootstrapping (Van der Meulen et. al 2007 and Crammer 1986) is used to control the statistical significance of

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differences in R^2. *** = 1% statistical significance, ** = 5% statistically significant, * = 10% statistically significant.

VIII. Conclusions

The IASB creates the standards and the conceptual framework in an attempt to create higher quality financial statements. Through this article, the extent to which this objective has been achieved is examined. Specifically, whether the quality of the financial statements of firms adopting IAS is superior to the period after the adoption of IAS, as compared with the period before the adoption, is the object of examination.

An important characteristic and a notable contribution of this research is the fact that the quality measurement methodology used, varies greatly from other existing methodologies that are identified in the existing literature. Specifically, through this article the quality of financial statements is detected in light of the Conceptual Framework. Particularly, the two fundamental qualitative characteristics set by the IAS Committee through the Conceptual Framework are examined in much detail.

The sample with respect to the specific research question consists of listed companies of fifteen European countries that have adopted IAS mandatorily. The countries included in the sample include Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden and the UK. Finally, the time horizon that is considered is 10 years, from 2000 until 2009. Specifically, the period between 2000 and 2004 is defined as the period before the adoption, while the period between 2005 and 2009 is defined as the period after the adoption.

Generally, the findings obtained support an increase in the quality of the financial statements of firms adopting IAS and are summarized as follows: First, an increase of the degree of relevance regarding the financial statements for the period following the adoption is identified. That increase is detected through the use of two alternative measures and suggests an increase in the quality of financial statements. Second, a marginal increase in the reliability of the financial statements is identified, without being statistically significant nonetheless. These results suggest that the degree of reliability of the financial statements did not change during the IAS transition of the countries under study.

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Appendix 1- Statistical significance of the differences of Factor Determination (R^2)

The methodology carried out in order to identify the statistical significance of the difference between two Coefficients of Determination (R2) was held in two steps. Initially, the standard errors as well as variations of the coefficients of determination for each sample were calculated using the 'bootstrapping' technique. Then, following the statistical test used by Van der Meulen et al, in 2007, which was based on the analysis of Crammer (1987), the statistical significance concerning the differences in terms of R2, was identified.

Specifically, the comparison of R2 between the two samples (prior and post the adoption), is performed through the following statistical test:

$$T=\frac{|R^2_{IFRS}-R^2_{LOCAL}|}{SE(R^2_{IFRS}+R^2_{LOCAL})}$$

Moreover, the standard error (SE) is equal to:

$$SE(R^2_{IFRS}+R^2_{LOCAL}) = \sqrt{VAR(R^2_{IFRS}+R^2_{LOCAL})}$$

Therefore, given that the two samples being independent, the following applies:

$$SE(R^2_{IFRS}+R^2_{LOCAL}) = \sqrt{VAR(R^2_{IFRS})+VAR(R^2_{LOCAL})}$$

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CURRENT TENDENCIES IN ENTERPRISE PERFORMANCE MEASUREMENT AND THEIR LIMITATIONS

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Abstract

The purpose of this research is to identify and present the latest trends in enterprise performance measurement, assessed specifically from financial point of view, respectively to provide details on the financial performance and to highlight their limitations, as well. The research is fundamental type. The Thomson Reuters Web of science database was used in order to find articles dealing with the topic of this research. The contribution of this research is the identification of the current tendencies in enterprise performance measurement, as given by a variety of empirical scientific publications on this topic, during the recent years, namely the company performance measurement and its explanation using the simple or multiple linear regression. The related limitations generated by the application of these regression equations resulted for each study sample is to be presented, as well.

Keyword: measuring enterprise performance, financial performance, measurement, influencing variables, uncertainty

JEL Classification: M40

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I. Introduction

The measurement and the evaluation of the enterprise performance is a topic of major importance, due to the fact that the performance of an economic entity is not a new concept, but the focus of many researchers, practitioners, business holders, potential investors, lending institutions, etc.

Nowadays, both theorists and practitioners in this field are interested in optimizing the results of any activities undertaken in all companies preparing annual financial statements.

Currently, the most recognized and applied methods of performance measurement of a business, as per economic and financial literature (Colasse Bernard, 2009, Gh. Vâlceanu & all, 2009, Bătrâncea & all, 2012, Monica Petcu, 2009, Petrescu Silvia, 2004, Marian Siminica, 2008, etc.) are the deterministic models, of causality.

But academia is concerned, within the last two decades, about the study of the company performance measurement in terms of applying of the stochastic models, as presented in a recent study "most of the empiric researches regarding the enterprise performance emphasize the analysis between the financial performance, highlighted by a measurement indicator, which is routinely a financial rate and some systematic variables which are considered by every paper (scientific researcher) relevant for their study and which more or less influence the performance of a company" (Deac V., Hlaciuc, E., 2014).

In this research, we aim to identify and present the latest trends in enterprise performance measurement, assessed especially from financial point of view, respectively the financial performance, and to highlight their limitations, as well.

This study contributes to the accounting literature by presenting and describing of the recent trends in company performance measurement, which is to be treated within the first part of this paper, and by presenting and explaining the limitations of these tendencies, as well, in the second part of the paper.

II. Current tendecies in enterprise performance measurement

The Professor Andy Neely, from Cambridge University, world widely recognized for his work in performance measurement, have presented in one of his researches, in 2005, that "the performance measurement is immature with little consensus" (Neely, A., 2005), and that "the performance measurement is not and cannot be a field of academic study because of its diversity" (Neely, A., 2005) – being studied in terms of various disciplinary backgrounds, such as accounting, informational systems, operational management and operational researches – however, the authors of these researches are in search of solutions to be addressed to a common challenge, namely how to ensure a performance measurement related to an entity strategy.

Why have we chosen the debate on this research? Because it complements the personal beliefs which will be further provided, on the one hand, and, it is a strong point of the international literature interest on this subject, on the other hand.

Thus, if in 2005, nine years ago, not even a decade, the Professor Neely shows that the performance measurement field was immature and that the researches undertaken over the years have not reached a common consensus, we can state that, currently, in 2014, the actual state of knowledge of the enterprise performance measurement is still under ongoing debate and development.

Though recently, the studies on performance measurement, have been trying to discover new models of performance measurement resorting to the methods, the techniques and the tools made available to researchers by econometrics. Besides, "the theory is a basic component of econometric studies, but it has to be developed into an usable form. The most common form for the purposes of econometrics is the one of a model, particularly an econometric model" (Albu, Lucian-Liviu, 2014).

In this respect, currently, the most empirical researches seek to discover and to build an econometric model that reflects the correlation between the financial performance (as financial indicator for its measurement) and certain systemic variables that are considered by each paper relevant to their study and which influence the performance of an enterprise.

The importance of using of the statistical, mathematical and econometric methods and models at the economic agent level was argued by other authors as well (Anghelache, 2010) trying to highlight the opportunities that "such a system of indicators provides for economic- financial complex and relevant analyzes".

We also note that the trend is induced by many empirical studies both nationally and internationally, which have used the methods and techniques made available by the econometrics discipline in order to reflect through a simple linear or multiple regression equation the link between the company performance or financial performance and one, respectively, more independent variables.

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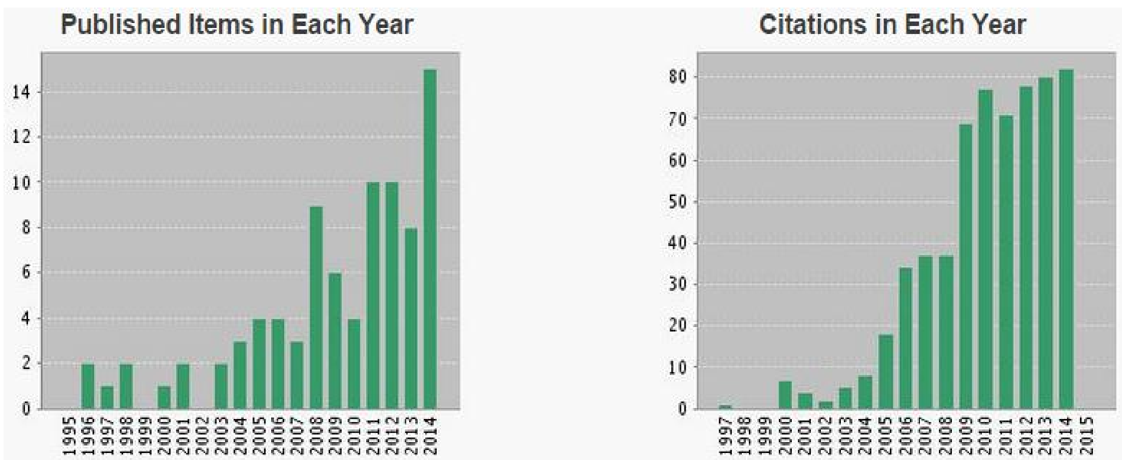
The emerging trends in the enterprise performance measurement are learned from the literature in the field of business economics. We called them “recent” because the works that we cite below are published within the last 5-6 years, we believe that they are recent works.

In this regard, Figure 1 shows the trend of the articles published between 1995 to 2014, in the database Thomson Reuters Web of Science, on "Financial performance" and "linear regression" in the area of Business Ecocomics.

Figure 1 - The evolution of the scientific articles published with topic like "financial performance" and "linear regression" in the area of Business Economics



Source: Thomson Reuters Web of Science

A total of 87 scientific articles were published during this period, with an average of 7.01 citations per article. As presented in Figure 1, since 2008, a strong growth in the number of articles published has been recorded, which shows a greater interest of academics in the topic presented. So, in order to sum up this tendency, we select some of the latest articles published since 2008. These are presented in Table. 1, which includes also the articles authors, the year of publication, the main theme of the study, and the sample used by each publication.

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Table 1 - Synthesis of the published articles in the period 2008-2014

Authors	Year	Main theme of the study	Sample used
Hsu, CC & all	2008	the effects of information sharing capability on buyer-supplier relationships and firm performance.	a set of survey data from the USA, Europe and New Zealand
Prado-Lorenzo, JM and all	2008	to analyse corporate social responsability practices implemented by Spanish companies and the relationship between such practices and corporate financial performance.	Spanish companies
Toyli, J., Hakkinen, L., Ojala, L., Naula T.,	2008	To explore the present logistics performance and to analyse the relation between logistics performance and financial performance.	424 Finnish small and medium sized enterprises in 2006
Doucouliagos, H.,, Laroche, P.	2009	The effect of unions on profits	forty-five econometric studies that report 532 estimates of the direct effect of unions on profits.
Garcia-Castro, R., Arino, M.O., Canela, M.A.,	2010	The empirical relationship between a firm's social performance and its financial performance	Panel data using 658 firms for the years 1991-2005
Markic, M. and al.	2011	the state of innovation policy and its influence on the successfulness of micro and small companies in the Republic of Slovenia	121 micro and small companies
Psomas, EL. and all.	2013	ISO 9001 effectiveness as the achievement of the standard's objectives and determine its impact on the performance dimensions of service	100 ISO 9001:2008 certified service companies

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		companies related to product/service quality, operational and financialperformance.	
Dhaouadi, K.	2014	the effect of human capital on the financial performance	most admired American firms
Huo, Baofeng and all	2014	the effectiveness of various supply chain integration (SCI) practices under different competitive strategies in terms of cost leadership and differentiation on financial performance	604 Chinese manufacturers
Yang, Y-F., and all.	2014	the effects of service innovation on financial performance	9220 proprietorship audit firms in Taiwan, 1989-2009 Survey Report of Audit Firms in Taiwan
Fernandes, CI. and all.	2014	the drivers to company innovation and their effects on the financial performance	sample of companies, from Portugal and Spain
AL-Qudah, Mustafa A.A.	2014	to identify factors that have impact on the financial performance (size of the company, the institutional investor, debt ratio, company age, liquidity ratio, customer satisfaction, productivity, degree of financial leverage	78 Jordanian industrial corporations for the years 2008-2012
Albertini, E.,	2013	The relationship between corporate environmental performance and financial performance	52 studies over a 35-year period between 1975 - 2011
Ruester, S., Zschille, M.,	2010	The impact of governance structure on firm performance	A data base using 765 water distriution firms from Germania
Lahtinen, K.,	2008	The effects of cost and value-added	27 large and

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Toppinen, A		components on the firm-level financial performance	medium-sized Finnish firms in 2000-2004
Ujunwa, A	2012	The impact of corporate board characteristics on the financial performance	Panel data from 122 quoted firms in Nigeria between 1991 and 2008
Gentry, R.J., Shen, W.,	2010	The relationship between financial performance (ROA, ROE ROS, ROI) and market performance	11.809 listed firms in U.S. for the years 1961 - 2008

Source: own projection.

Following the recent trends presented with regard to the company performance measurement, especially in the measurement of financial performance, we consider that they are represented by empirical studies that investigate, by means of the linear regression, the correlation between certain influencing variables and the financial performance. The diversity of the influence factors considered relevant by each researcher for his study can be seen in table no. 1.

III. The limitations of the recent trends in enterprise performance measurement

This method of measuring of the company's performance can be of an emphasized importance, method rated as "recent trend", due to the fact that these econometric models are probabilistic models of stochastic nature. In such a model, the exact value of the resulting variable Y cannot be determined, based on knowing of the value variable X (variables Xi), so that the model is transformed from a deterministic model into a stochastic model, which involves a random variable, usually denoted by the symbol ε.

Based on this argument, we can continue our advocacy, as we want to describe the main limitation of these recent trends of enterprise performance measurement. Also we will argue why it is necessary to study the uncertainty in measuring of enterprise performance.

We believe that one of the major limitations of the recent trends of enterprise performance measurement is represented exactly by the influence of uncertain factors over it. While many different aspects of the certain variables introduced into a model of enterprise performance measurement are detailed in the economic literature, as we have shown above, little is known about the uncertain side, namely the random variables, the place, the role and their impact on companies performance.

As long as the stochastic models used for the enterprise performance measurement are applied in order to achieve predictions that meet the decision making of the management of the economic entities in order to improve its quality, considering that better decisions, more reliable ones lead to better results in future – it involves as well, an uncertain side of disturbing factors that may have various influence from one economic entity to another, we believe that they cannot be used with the utmost precision in business.

Therefore, in order to improve these models as ready to be used in practice with a greater accuracy and precision, we consider studying of the uncertain nature, explained through random variables that affect the performance of the company as absolutely imperative.

IV. Conclusions

In this paper, we have identified and presented several scientific publications in the field of economic business with the main topic of company performance measurement and its influencing factors - publications considered as compounding the "recent trend of measuring the company's performance".

"If the classical economists believed that for a company to develop economically and to produce more it was sufficient to increase the amount of available factors, labour and capital, nowadays it is estimated that the most important role in the economical growth is held by the progress registered in the scientifical knowledge and technique" (Petriş R., Hlaciuc, E., 2010). A progress in scientific knowledge of the enterprise performance measurement would be the studying of these random variables, in terms of probability theory, of econometrics and of all of the modern tools and methods provided by these scientific disciplines.

In conclusion, we can affirm that the contribution of this research is the identification of the current trend in enterprise performance measurement, as given by a variety of empirical scientific publications on this topic, during the recent years, namely the company performance measurement and its explanation using the simple or multiple linear regression and the presentation of the limitations generated by the application of these regression equations resulted for each study sample.

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IMPACT OF FINANCIAL CRISIS ON FINANCIAL AUDIT ACTIVITY IN ROMANIA

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Abstract

Given the growing concerns in the current socio-economic context for obtaining more relevant and more „insuring" information on the quality of financial information provided by the financial statements of various companies, both practitioners and academics, but also regulators, are asking various questions on how external audits and audit reports are and should be looked at.

Unfortunately, in recent years we face a continuous degradation of the audit image, and by default of that of financial auditors. This is due to scandals and bankruptcies of companies and financial institutions, where auditors have contributed more or less. All these led to intensified efforts of audit professional and regulatory bodies for analysing the causes of these phenomena in order to identify and impose a number of measures aimed to restore the lack of credibility occurring increasingly stronger in the results of auditors' work.

Auditors and audit companies should not overlook the social importance of financial audits in recent years – a position obtained after an effort of hundreds of years - and eventually extend their responsibilities and seek for new methods or procedures compatible with current needs in order to support their work. Therefore, audit value must be continually tested against requirements of users and society. Accounting profession must build a solid case in favour of the benefits brought by audits to business, economy and society.

Audits must evolve and expand to add more value for users. Especially for listed companies and even more in times of crisis, audits must be more than an opinion on historical financial statements.

Keyword: financial audit, financial crisis, credibility, perceptions, audit report

JEL Classification: M42, M01, G01

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I. Introduction

In an increasingly integrated economy, *accounting information*, respectively its *credibility, relevance and integrity,* still are issues frequently studied by experts. In this context, we believe that research conducted so far have been performed from the standpoint of accountants as producers of information or from the perspective of its users, and *less from the standpoint of auditors*, who ensure the integrity and credibility of financial information against fraud.

The need for accurate and relevant information has always existed within all economic, social or any other activities, but its importance became evident in the last decade, with the financial scandals that have involved a number of large corporations. All these events have had a strong impact on the global economic market, outlining the possibility for some investors to fully lose confidence in investments made by companies, but also in their management.

In this context, *the role of financial auditors becomes very important*, namely to provide credibility to financial information in order to ensure a decision-making process based on accurate information, the functioning of cash-flows on capital markets and of economy as a whole.

In terms of the gap between users' perceptions and expectations on the audit, because lately the economic crisis deepened in Romania also appeared a number of articles and studies that emphasize the *importance of the work of auditors, but also its relevance for the public interest*. These refer to the proposed models on the perception gap related to audit independence, for a greater awareness of auditors, regulators and the public of the risk of the existence of such gaps with adverse effects on the image of auditing profession (Ţurlea & Mocanu (2010)). Other studies deal with interdependence relationships and direct effects of auditors' independence on their performance (Jaba & Robu (2011)), the role of external audit in insuring credibility of audit reports (Dobroţeanu et al. (2011a)), degradation of perceptions and gaps between expectations and needs before and after the start of the financial crisis (Dobroţeanu et al. (2011b)), the link between restoration of public confidence and decrease of expectation gaps in terms of public interests (Ardelean (2013)).

The role and relevance of information provided by auditors to the public through audit reports is therefore a controversial topic, which in recent years has generated lots of discussions among experts and practitioners. *The risks to which users of information provided by auditors are exposed to have increased*, and also *diversified* considerably, due to the economic changes caused by the global crisis. Companies' attempts to embellish results and present a distorted image of financial statements also hinder auditors' activities for obtaining reasonable assurance. It is considered that an audit report containing a favourable opinion is in fact a business card that can facilitate new business opportunities for the audited company.

II. Research methodology

This article can be structured into two main parts. The first part is dedicated to ***fundamental research***, containing a number of debates and standpoints about the financial crisis as a fundamental concept, respectively its impact on accounting theories and practices. The second part is reserved for ***applied research***, where we intend to put face to face the perceptions of the two groups about the impact of financial crisis on audit activities and profession in Romania.

By its nature, this article is part of the ***positivist research trend*** with extensive *interpretative approaches*, and with a number of *critical elements* and many *personal opinions*, which intertwine harmoniously and give the article a touch of originality and professionalism. The article's quality is also ensured by the large number of charts, structural schemes and tables used, whose purpose is to facilitate understanding the information presented in this research.

In terms of generated information, this research combines ***qualitative research*** (most investigated items are of qualitative nature) with ***quantitative research***. The two types of research are not antithetical but complementary, since in our view, a scientific approach that will stand the test of time requires an optimal combination of research methods in order to achieve the aimed objectives.

The research follows a *transverse direction* through the used *observation, comparison* and *conceptual analysis* techniques. Thus, the qualitative research valued specialist literature by processing it with various *methods specific to socio-human sciences*, such as *document analysis*, *non-participating observation* and *comparison*. The non-participating approach is due to the research field and the current state of knowledge in the field of interest, although comparisons made and opinions and conclusions

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expressed show certain participating aspects of the research, respectively the relevance of transmitted information.

In our opinion, the dynamics of analysing scientific literature is relevant in the analysis of audit evolution, and consequently for increasing complexity of tasks and responsibilities attached to financial auditors, the more that we talk about periods of financial crises. The sources used are mostly scientific articles published in specialist magazines in the field of financial audit.

The last part of this article is part of the ***positivist constructive research trend,*** and the purpose of the ***empirical study*** is to value the information discussed throughout the scientific approach, by testing and dimensioning the main gaps related to managers' and auditors' perceptions on audit activity in the context of a sensitive socio-economic climate, characterised by instability and turbulences. To accomplish this task we used the ***questionnaire method***. The questionnaire was applied to active financial auditors from Romania, but also to managers of audited companies. By applying this questionnaire we aimed to test the consistency between the perceptions of the two groups about the impact of financial crisis on audit activity and credibility of financial auditor profession.

As we shall see, our assumptions contain a selection of factors we wanted to test. This selection is necessary because specialist literature shows a large number of elements whose validation through a single study would have been exhaustive and practically impossible.

III. The impact of financial crisis on accounting theories and practices

Currently, the socio-economic environment still goes through a difficult situation, namely the global financial crisis that began since late 2007. In this respect, A. Einstein pointed out that: *„It is in crisis that invention, discovery and large strategies are born"* (from Mâţu, Ş., Buneci, P., Gheorghe, V. (2009), *Criza, anticriza şi noua ordine mondială,* Solaris Print Publishing House, Bucharest). This crisis implicitly „pulls" the alarm on production and procurement, but especially certification and use of financial information that have an important role in preventing, reducing or fighting such difficult situations.

The central concept of this article is the *financial crisis,* which concerns all stakeholders, calls for reconfiguration of economic philosophies and of the dominant logic

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and requires strategies for exiting the state of economic decay, tactics for controlling aggregation effects, dismantling of immobility and enhancement of stimuli.

The general global economic crisis and the financial scandals at large companies (Enron, WorldCom, Ahold, Parmalat, etc.) call again into question the ***quality and reliability of financial information***. Thus, the world's globalisation issues are reflected also on the evolution of accounting and auditing professions. Globalisation of world economy amid a global economic crisis creates new situations and doubts on everything related to the economy of each country.

These developments in the economic-social environment have often been improperly associated with the *accounting profession*, which is responsible for defending public interest by means of correctly informing external users, respectively guaranteeing credibility of data published by companies. For example, in recent years, ethical failures by certain members of the profession, which resulted in a lack of confidence in financial reporting, required significant changes in the rules of the profession (Sarbanes-Oxley Act in USA, Financial Security Law in France, etc.), as documented in their study by Toma & Potdevin (2008: 33).

In our opinion, amongst the representatives of accounting profession, financial auditors are most exposed to virulent criticism coming from users of information within financial reporting. They are considered *„scapegoats",* as guarantors of quality and reliability of data disseminated by companies. Sometimes, it goes even further, considering that these professionals are *solely responsible for the failures faced by large companies* or groups of companies. Therefore, in our opinion, the reputation and responsibility of the financial auditor profession are directly influenced by the qualitative features of financial information, compliance with rules imposed by the accounting referential, and with principles of ethical and professional conduct.

In this context, the role of the auditor increases, *„its value must acquire new levels by providing additional elements related to transparency of operations, the need of an increased vigilance towards complex financial products and the need to better understand both individual and systemic risks"* (PhD Professor Ion Mihăilescu, President of CAFR [Chamber of Financial Auditors of Romania] – interview / The 2nd Congress of the Financial Auditors of Romania: *"Naţional şi internaţional în activitatea de audit financiar. Auditorii şi criza economică globală"* [National and International in Financial Audit. Auditors and the Global Financial Crisis], 2009). Professional accountants are required to make the necessary adjustments related to the way of reporting financial

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indicators, and for a more accurate understanding of situations by users. Thus, the importance of auditors will increase, because both creditors and investors, but also the large public, rely on their opinion of independent experts.

Thus, we, as auditors, should be concerned of identifying solutions for *regaining investors' confidence*, by identifying liquidities, because they do exist, but not at the right places. Auditors „see the financial reporting and activity of a company from two standpoints: information accuracy and going concern. Auditors should collect a sample of required, sufficient and appropriate evidence, so that in short time they can provide a relevant opinion resulted from the audit report. The report as a whole, and in particular the paragraph related to going concern, is one of the elements that support business environment and, corporate management" (PhD Professor Ion Mihăilescu, President of CAFR [Chamber of Financial Auditors of Romania] – interview / "Atât auditorul, cât şi clientul acestuia trebuie să se subordoneze unor valori etice" [Both the auditor and the client must be subordinated to ethical values], Economistul [The Economist] newspaper, 2009).

The question is, *how do we proceed as auditors, how do we overcome the crisis and what do we learn out of that?* In our opinion, the answer lies is how auditors, as accounting professionals, perceive the concept of *fair value* and perform the audit of the balance sheet, in how they identify and report *fraud*, respectively the *going concern audit*.

IV. Financial auditors' responsibilities to the challenges of financial crisis – convergence between theory and practice

The global financial crisis that lasts for some time already and does not show clear signs of an end, aroused acute concerns not only related to causes – which were discussed under all possible aspects – but especially to the real recovery and revival chances. In particular, the most appropriate mechanisms are sought for restoring trust in business and for creating a fair and predictable commercial and financial climate.

Inevitably, when looking for appropriate solutions hopes are related to the *potential offered by information obtained through financial audit*, which is recognised to have an increasingly prominent social role in ensuring business health. And it is not just about opinions on what is expected from auditors, but also about specific actions, which –

as we saw – took the form of discussion papers for the preparation of measures considered necessary to be adopted.

Fact is that now financial audit is on the verge of a reform to better meet the challenges of the period we are going through. In our opinion, currently, audit is a global service, whose effects are felt throughout all economic fields and with cross-border impact. However, greater *public awareness of the objectives and scope of an audit would be necessary,* given that *public awareness deficiencies can cause deficiencies related to the public's expectations from auditors*.

There is a consensus that the *social role of auditors and audit profession* should action in the context of *protecting public interests*. Thus, the public must gain a proper understanding of the audit profession and not generalise it to believe that the auditor is a *factotum*, a god, an omniscient that can also do very long-time predictions.

The „Green Book" of audit, a discussion paper issued by the European Commission, even contains an attempt to charge auditors with a pretty unpleasant duty, namely to *make clear specifications on the period in which it is more likely for the audited company to resist*. This is very difficult, if not impossible. Not even rating agencies – which have mathematical techniques and statistical models – can do this. *What could an auditor do, who studies some situations related to the past?* He may issue an opinion, but cannot predict an exact period for the company's sustainability for more than one year, according to the going concern principle.

Given its impact on various stakeholders, *audit profession is very sensitive*. Thus, regulations and rules adopted domestically or internationally ought to be judiciously based on extensive research and market studies. It is necessary for the large public to gain a proper understanding of the audit profession in order to have reasonable expectations. On the other hand, the *profession is called to properly respond, to adapt as good as possible to the requirements of the current period*. Therefore, financial auditors are bound to be in a position to build confidence in both auditors and their professional body, the Chamber of Financial Auditors of Romania, first of all by the quality and accuracy of services provided by its members.

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V. Analysis of respondents' perceptions on the impact of financial crisis on audit activity

In our opinion, theoretical research, as important as it would be, is not enough in the current socio-economic context. Today, more than ever, it is necessary to get closer to economic reality – and for this reason empirical studies have increased lately.

Therefore, our study is also an empirical descriptive one, based on a *questionnaire* that aims to value theoretical-methodological elements presented in previous chapters.

The aim of our research is to *compare external perceptions (public interest) with auditors' own perceptions about the impact of financial crisis on financial audit activity in Romania*. We considered seven elements, as following:

A. Auditors' turnover in 2008, before the actual outburst of the crisis, compared to 2012, a year characterised by crisis effects;

B. Fluctuation of auditors' fees since the outburst of the crisis;

C. Difficulties faced by respondents during external audit engagements attended in the last five years of economic crisis;

D. Changes occurred in the type of opinion issued by auditors for financial year 2012 compared to financial year 2008 at audited companies;

E. Weight of unqualified opinions, qualified opinions, respectively modified opinions (adverse and/or impossibility to express an opinion) in the total audit reports issued on 31.12.2008 compared to 31.12.2012;

F. Impact of adopting IFRS correlated with the impact of financial crisis on audit engagements;

G. Influence of financial crisis on fair presentation of financial statements and on workload both for the preparation and auditing of annual financial statements.

By means of the above, we start validation of our assumption: ***„H: The financial crisis has had an impact on the activity of financial auditors in Romania."***

Thus, by means of quantitative research, this empirical study aims to *analyse and size the gap between auditors' perceptions about the impact of financial crisis on the audit activity compared against the perception of managers of companies that require external audit services*.

Thus, the primary objective of this study is to *provide evidence on the perception gap in Romania between auditors and audited companies, by means of investigating their*

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perceptions, opinions, needs and expectations, respectively to highlight the impact of financial crisis on the credibility of the audit profession.

A. *Analysis of respondents' (auditors) perceptions about the impact of financial crisis on the turnover of the company they work for*

Further to a simple analysis, we note that most auditors have stated that their turnover for 2012 has declined considerably compared to the turnover for 2008. Thus, both in 2008, and in 2012, the largest share is represented by financial auditors with a turnover between EUR 100,000 and 250,000 EUR, but the weight is of 47% in 2008, respectively 42% in 2012.

Table 1 - Comparison between turnovers registered by companies in 2008 and 2012

	2008	%	2012	%	Difference 2012 compared to 2008
Below EUR 20,000	27	*17%*	26	*16%*	*-1%*
Between EUR 20,000 and EUR 100,000	37	*23%*	47	*29%*	*6%*
Between EUR 100,000 and EUR 250,000	76	*47%*	69	*42%*	*-5%*
Between EUR 250,000 and EUR 500,000	12	*7%*	14	*9%*	*2%*
Over EUR 500,000	11	*7%*	7	*4%*	*-3%*
TOTAL	163		163		

Source: own projection

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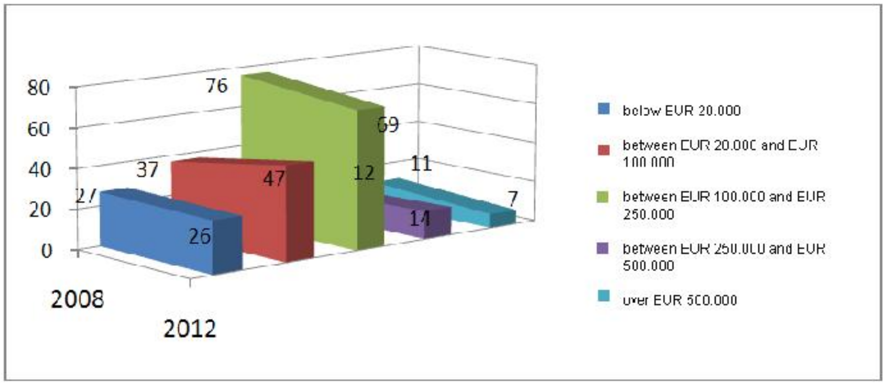
Chart 1 - Split of respondents (auditors) by their perception of the impact of financial crisis on turnover



Source: own projection

Because the data above were relevant, but not sufficient, respectively did not allow us to issue a clear opinion on the impact of the financial crisis on turnover accomplished by auditors before the crisis (2008), respectively in full crisis (2012), we:

- Performed an effective assessment of the cases where turnover decreased, stayed at the same level, respectively increased, and
- Stratified the answers in order to effectively determine the magnitude of the increase or decrease.

Thus, as highlighted in the chart below, 70% of the respondents said that their turnover has remained approximately the same from 2008 to 2012, while only 12% enjoyed an increase in turnover. However, in 29 cases, respectively 18%, auditors' turnover showed a decreasing trend from 2008 to 2012.

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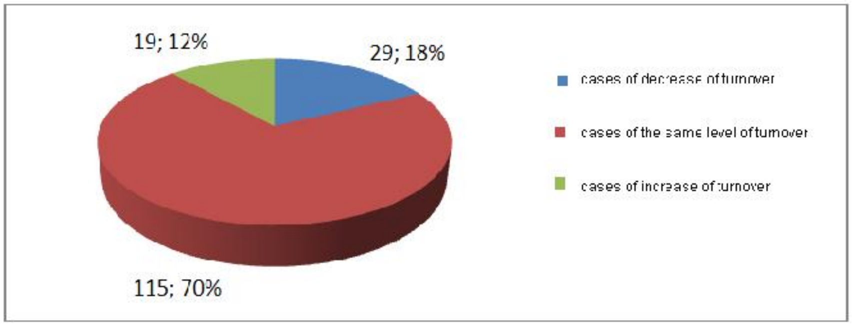
Chart 2 - Cases of decrease /same level/increase of turnover from 2008 to 2012



Source: own projection

The above chart shows the weight of cases where turnover decreased, increased or remained at the same level, and the following table presents a stratification of answers received in order to actually determine the magnitude of the increase or decrease.

Table 2 - Stratification of decrease, same level and increase cases in turnover in 2012 compared to 2008

Decrease in turnover in 2012 compared to 2008						
	2012					
2008		**Below EUR 20,000**	**Between EUR 20,000 and EUR 100,000**	**Between EUR 100,000 and EUR 250,000**	**Between EUR 250,000 and EUR 500,000**	**Over EUR 500,000**
	Below EUR 20,000	**-**				
	Between EUR 20,000 and EUR 100,000	**2**	**-**			
	Between EUR 100,000 and EUR 250,000	**2**	**13**	**-**		

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	Between EUR 250,000 and EUR 500,000	**1**		**6**	**-**	
	Over EUR 500,000			**1**	**4**	**-**
	TOTAL:	**29 people said that their turnover** decreased significantly in 2012 compared to 2008.				
Same level of turnover during the period 2008 – 2012						
	2012					
2008		**Below EUR 20,000**	**Between EUR 20,000 and EUR 100,000**	**Between EUR 100,000 and EUR 250,000**	**Between EUR 250,000 and EUR 500,000**	**Over EUR 500,000**
	Below EUR 20,000	**21**				
	Between EUR 20,000 and EUR 100,000		**29**			
	Between EUR 100,000 and EUR 250,000			**55**		
	Between EUR 250,000 and EUR 500,000				**4**	
	Over EUR 500,000					**6**
	TOTAL:	**115 people said that their** turnover remained at the same level from 2008 to 2012.				
Increase of turnover from 2008 to 2012						
	2012					
2008		**Below EUR**	**Between EUR**	**Between EUR**	**Between EUR**	**Over EUR**

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		20,000	20,000 and EUR 100,000	100,000 and EUR 250,000	250,000 and EUR 500,000	500,000
	Below EUR 20,000	**-**	**5**	**1**		
	Between EUR 20,000 and EUR 100,000		**-**	**6**		
	Between EUR 100,000 and EUR 250,000			**-**	**6**	
	Between EUR 250,000 and EUR 500,000				**-**	**1**
	Over EUR 500,000					**-**
	TOTAL:	**19 people said that their** turnover increased from 2008 to 2012.				

Source: own projection

B. *Analysis of respondents' (auditors) perceptions about the impact of financial crisis on the level of collected audit fees*

Also, we aim to identify the same quantitative feature of the sample, respectively to confirm – in conjunction with previously learned information – that the unstable socio-economic environment has had an impact on the average level of audit fees collected by auditors, and consequently, that the financial crisis indeed has a significant adverse impact by turning them downwards.

Based on the chart below, the highest weight (40%) is represented by financial auditors who stated that with the financial crisis outburst their average fee level decreased by 10-20%. 28% of the respondents stated that their fees decreased up to 10%, while 17% registered same levels or even an increase. Only 3% have faced a dramatic situation, where collected fees have decreased by over a third.

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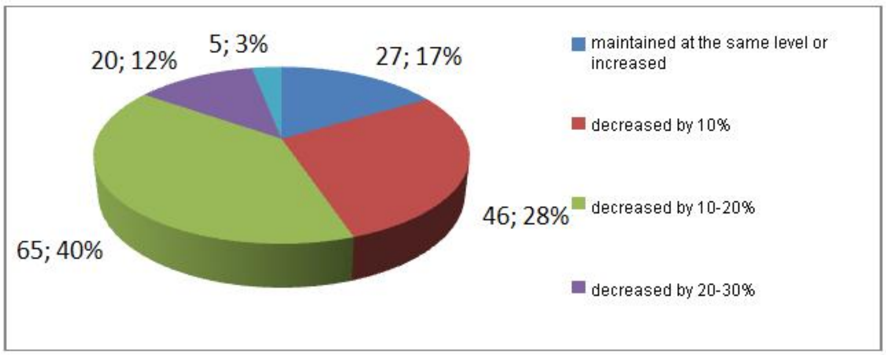
In this context, given the crisis conditions, it is clear that audit professionals felt the pressure to reduce fees.

Chart 3 - Split of respondents (auditors) by their perception about the impact of financial crisis on the average level of collected audit fees



Source: own projection

While global economy continues to struggle to get momentum, accounting practices in general find that pressure to reduce fees for the provided professional services continues to represent a significant challenge. This is one of the key messages emerged also from the May-June 2012 edition of the ***Quick Questionnaire*** (Giancarlo Atollini, President of SMSPIFAC Committee Cum facem faţă presiunii de a reduce onorariile? Sfaturi de gestionare a activităţii pentru P.M.M.-uri [How do we face pressure to reduce fees? Business management tips for SMSPs], http://ceccar.ro/ro/wp-content/uploads/2012/11/IFAC-SMPC-FEE.pdf) ***for SMSPs developed by IFAC*** (http://www.ifac.org/about-ifac/small-and-medium-practices-committee), which received 3,678 answers worldwide. When they were asked to name the biggest challenge faced by their small or medium-sized practice in this period of economic crisis, most respondents (27%) – particularly in Europe and Asia – mentioned the pressure to reduce fees.

While pressure on fees is nothing new, as the profession always faced some pressure levels, the perpetuation of bad economic conditions has likely contributed to increased concerns about the pressure of fees in many SMSPs.

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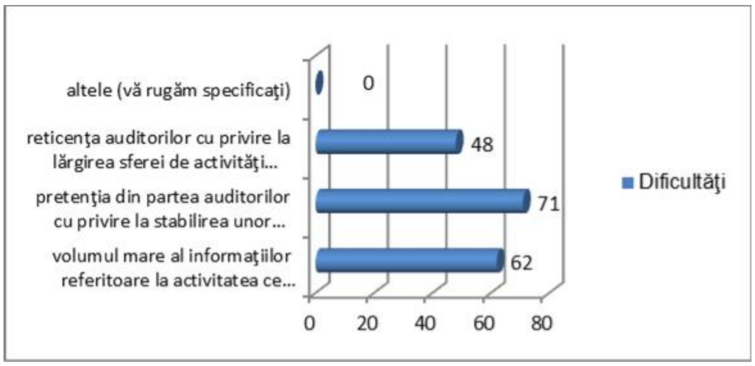
C. Analysis of respondents' perceptions about the difficulties encountered during external audit engagements attended in the last five years of financial crisis

Chart 4 - Split of respondents (managers) based on their perception about the difficulties encountered during audit engagements attended in the last 5 years of financial crisis



Source: own projection

The semi-open question regarding potential difficulties faced by managers during audit engagements attended in the last five years of financial crisis allowed respondents to choose 2 or 3 variants out of our predetermined answers, according to their importance, respectively to specify another possible difficulty they have faced.

More than half of those who answered our questionnaire stated that *„auditors claimed higher fees"*, which only confirms the above.

We believe that this perception of managers of companies using audit services comes from the fact that they are possibly facing low demand for their products and services. Considering that everyone is looking at reducing costs, it is no surprise that audit companies are facing requests for fee negotiations or price reductions, while at the same time they are asked to maintain same quality of services.

Out of various reasons, this increased pressure on fees threatens to become a new standard that will last long after the global economy will have recovered. Firstly, clients may decide to keep their bills low and may consider that no professional services, including legal, accounting or audit services, are not worth the fees paid before the economic crisis. Secondly, globalization and low cost benefits of outsourcing of services to cheaper foreign contractors could make clients to ask for part of the cost savings.

Another complaint of managers is linked to the *„high volume of information on*

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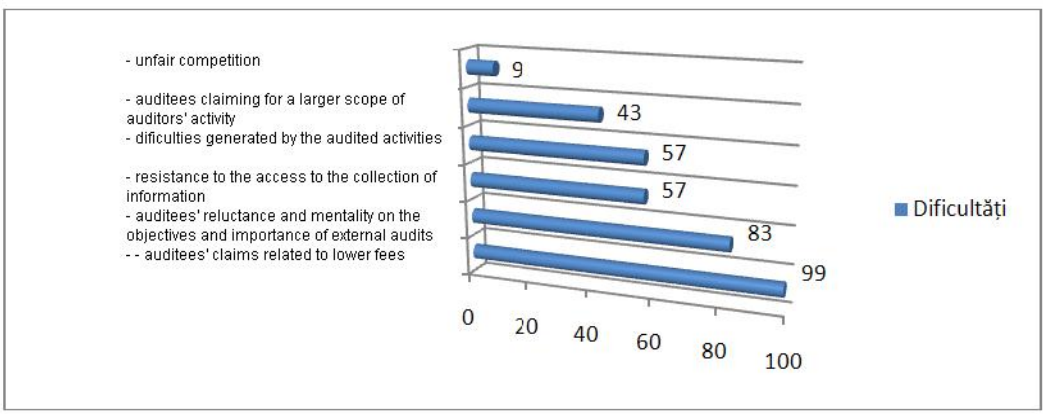
the activity to be audited, which are requested by auditors", 62 of them being intrigued by this and considering it maybe a hindrance in carrying out their daily activities. For any audit practitioner it is well known that managers often „complain" that too much information and too many documents are requested during the audit, that all members of the financial-accounting department must „be available" to the audit engagement team. However, it is management's duty and responsibility to ensure auditors' unrestricted access to any type of information and documents requested for the proper development of the audit engagement.

It is also interesting that one third of respondents are disappointed of *„auditors' reluctance for broadening the scope of their activity"*. In this case, we either talk about a greater need („innocent" by the way) for relevant information in order to make business administration decisions or about a strategy for reducing consultancy services costs in general, based on the „all inclusive" principle. In our opinion, both variants are possible, given the sensitive socio-economic context, but also the big gap between the expectations of the users of audited financial statements and actual performance of auditors, as we shall see below.

Chart 5 - Split of respondents (auditors) by their perception about difficulties faced during audit engagements attended in the last 5 years of financial crisis



Source: own projection

On the other hand, auditors seem to be dissatisfied at a rate of 61% (respectively 99 of them) with the *„audited companies' claims related to lower fees"*.

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Thus, this is confirmed for the third time in this study. These sources of pressure on fees occurs in Romania as well, and the closure of many companies due to the economic crisis increases the pressure on audit and accounting professionals for providing services at the lowest possible prices. Some professionals were (and are!) ready to accept a significant decrease of income hoping to keep old clients or gain new clients.

However, it seems that in one way or another, this strategy has affected the quality of provided professional services. Regardless of whether the pressure to reduce fees is a temporary or a medium or long-term phenomenon, audit professionals should respond to this constraint while maintaining the quality of the provided services.

On the other hand, 51% of the respondents, respectively 83 auditors, mention as an obstacle of high importance the *"audited companies' reluctance and mentality on the objectives and importance of external audits"*. We will try to confirm this by analysing the answers of managers to the questions in the following section, which focus on their perception about the function, object, scope and usefulness of financial audit.

Especially after having said the above, it is not surprisingly that about one third of the auditors felt resistance from managers related to the *access to the collection of information on the activity of the company to be audited*. Also, auditors state that managers *"claim for a larger scope of their activity"*.

However, it was unexpected that 9 surveyed persons, who had the possibility to provide an open answer to this question, different than the predetermined ones, gave the same answer, stating *"unfair competition"* as a hindrance in their activity.

D. *Analysis of respondents' (managers) perceptions about the impact of financial crisis on changing the type of opinion issued in financial year 2012 compared to financial year 2008*

The impact of financial crisis was also analysed in correlation with *changing the type of opinion for financial year 2012 compared to financial year 2008*. Managers were asked to indicate what type of opinion auditors issued for the financial statements as of 31.12.2008, respectively 31.12.2012.

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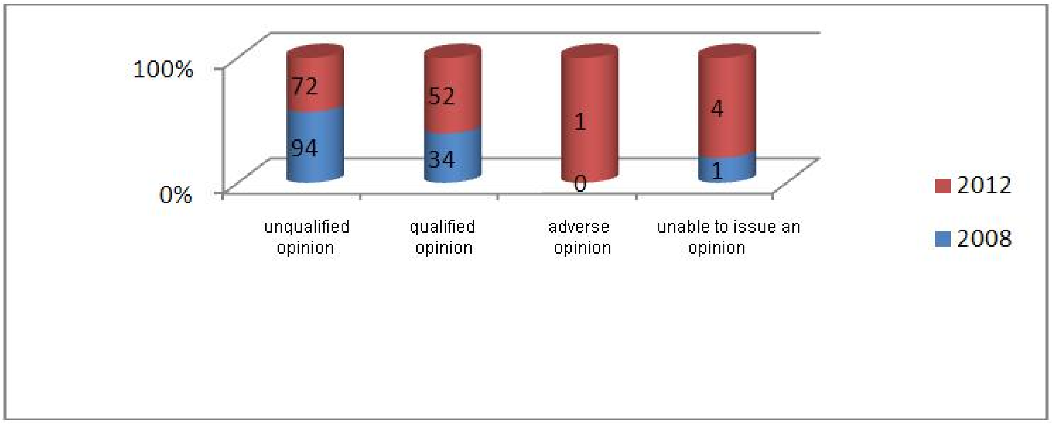
Chart 6 - Split of respondents (managers) based on their perception about the impact of financial crisis on changing the type of opinion for financial year 2012 compared to 2008



Source: own projection

After analysing managers' responses overall, we can say that the *number of unqualified opinions decreased considerably from 2008 to 2012,* from 94 to 72 (total of 129 opinions), while the *number of qualified opinions increased remarkably*, from 34 in 2008 to 52 in 2012, a year of full financial crisis. Also, in 2008 the auditor was unable to issue an opinion for only one company while in 2012 there were 4 such cases (out of the 129 cases), but also one adverse opinion.

E. Analysis of respondents (auditors) perceptions about the impact of financial crisis on the weight of unqualified, qualified, respectively modified (adverse and/or impossibility to issue an opinion) opinions in the total of audit reports drawn up on 31.12.2008 compared to 31.12.2012

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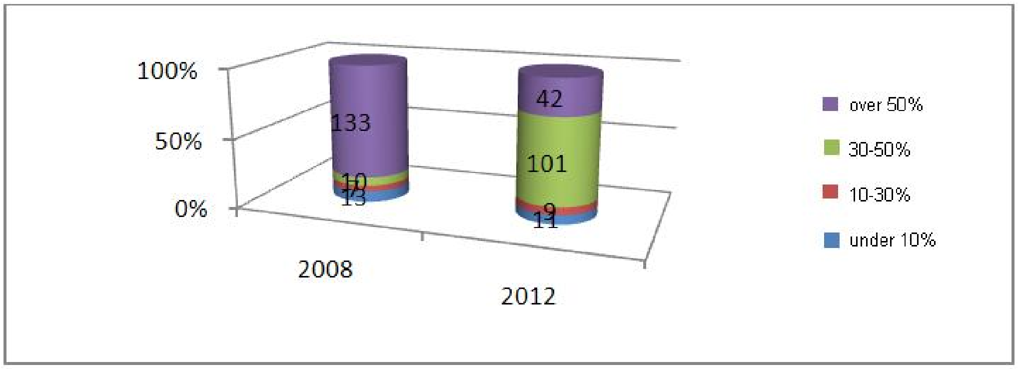
Chart 7 - Split of respondents (auditors) based on their perception about the impact of financial crisis on the weight of unqualified opinions in the total audit reports drawn up in 2008 compared to 2012



Source: own projection

By analysing the answers of auditors and the chart above we note that most respondents (133 of 169) stated that on 31.12.2008 the weight of unqualified opinions was over 50%, while 101 auditors said that the weight of unqualified opinions on 31.12.2012 stands between 30-50%.

In our opinion, the high percentage of unqualified opinions before the economic crisis is due to the fact that in general any qualifications expressed in the audit report generates a negative perception of users. We believe this was and still is one of current issues in this field. A paradigm „all or nothing" perpetuated, where qualifications in the audit report represent a taboo for both clients and auditors.

The question is whether this perception should be revised or shareholders and other users of accounting information should be really concerned about this issue. Fact is that we can say that due to the unstable economic environment auditors have given up this taboo and they are no longer so „generous" in issuing unqualified opinions.

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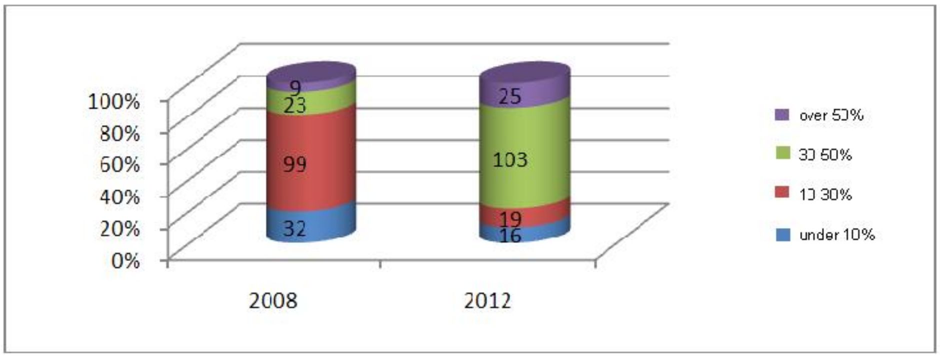
Chart 8 - Split of respondents (auditors) based on their perception about the impact of financial crisis on the weight of qualified opinions in the total audit reports drawn up in 2008 compared 2012



Source: own projection

According to the majority of auditors (respectively 99 of them), the weight of qualified opinions was between 10-30% on 31.12.2008 while on 31.12.2012 approximately the same majority of respondents (respectively 103 of them) assessed the weight as much higher, respectively between 30-50%.

Thus, we believe that due to the economic crisis, auditors have taken certain „measures" (both literally and figuratively!), being much more reluctant in issuing audit reports with „clean" opinions. Therefore, most unqualified opinions issued in reports drawn up for the financial year 2008 have been replaced by qualified opinions.

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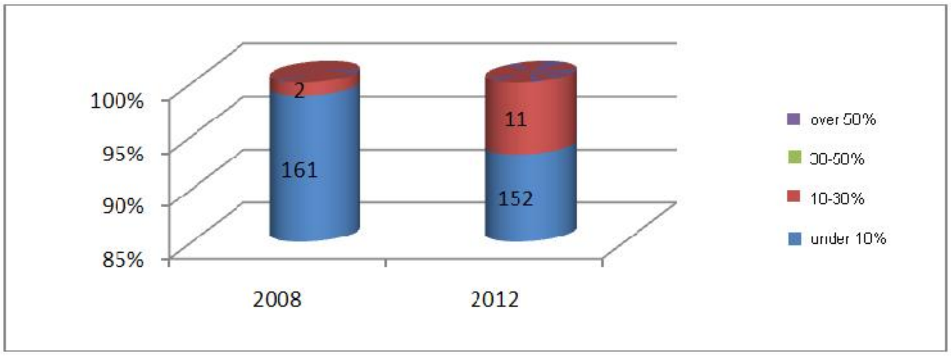
Chart 9 - Split of respondents (auditors) based on their perception about the impact of financial crisis on the weight of adverse opinions and cases of „impossibility" in total audit reports drawn up for 2008 compared to 2012



Source: own projection

Moreover, as we can see above, for 31.12.2008 only 2 respondents admitted that in 10-30% of the cases the audit reports contained either an adverse opinion or they were unable to issue an opinion while for 31.12.2012 there were 11 such cases.

F. Analysis of respondents' perceptions about the impact of IFRS adoption correlated with the impact of financial crisis on audit engagements

Next we aimed to determine the factor that most impacted the audit engagement according to the two groups of respondents: adoption of IFRS or the financial crisis

Table 3 - Perception of respondents about the impact of IFRS adoption correlated with the impact of financial crisis on audit engagements

		Total disagreement (1)	*Partial disagreement (2)*	*Neither agree or disagree (3)*	*Partial agreement (4)*	*Total agreement (5)*	**TOTAL**	**Average frequency**	**Standard deviation**	**Rank**
MANAGERS	Impact of IFRS on audit engagement	9	23	23	32	42	129	**3,58**	**1,30**	**2**
	%	*6,98%*	*17,83%*	*17,83%*	*24,81%*	*32,56%*	*100,00%*			
	Impact of crisis on audit engageme	8	18	27	32	44	129	**3,67**	**1,25**	**1**

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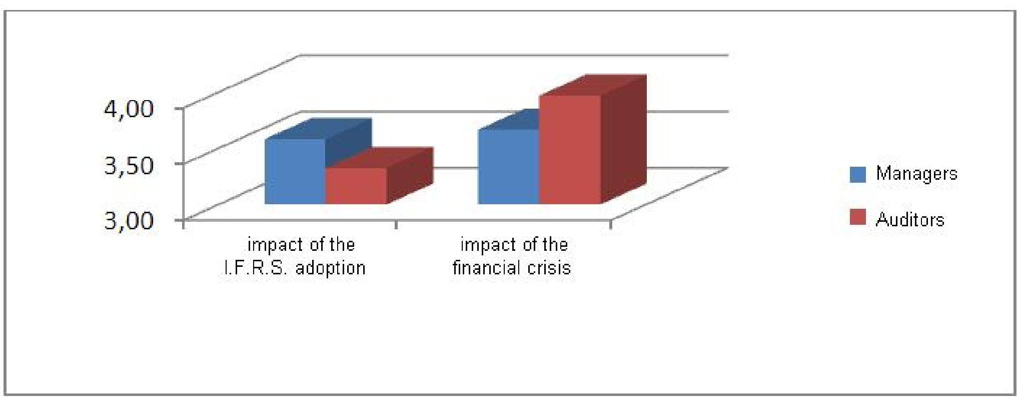
	nts									
	%	*6,20%*	*13,95%*	*20,93%*	*24,81%*	*34,11%*	*100,00%*			
AUDITORS	Impact of IFRS on audit engagements	2	8	105	31	17	163	**3,33**	**0,78**	**2**
	%	*1,23%*	*4,91%*	*64,42%*	*19,02%*	*10,43%*	*100,00%*			
	Impact of crisis on audit engagements	1	3	38	79	42	163	**3,97**	**0,79**	**1**
	%	*0,61%*	*1,84%*	*23,31%*	*48,47%*	*25,77%*	*100,00%*			

Source: own projection

If we were to make a hierarchy of factors that impact most the audit engagements – adoption of IFRS or the financial crisis – based on the table above we note that opinions are not divided. Both managers and auditors consider that *financial crisis had a greater impact on audit engagements than IFRS adoption*, but still an *average impact*, given the value of the average frequency of 3.67, which is considered a neutral opinion (based on the Likert scale). The values for the other factor are close to this value: 3.58, respectively 3.33, with plus or minus deviations between 0.78 and 1.30.

Chart 10 - Top of factors that have an impact on audit engagements – managers vs. financial auditors



Source: own projection

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G. Analysis of respondents' perceptions about the impact of financial crisis on the fair presentation of financial statements and on the workload for both preparation and auditing of annual financial statements

Another objective was to determine the most experienced effects of the financial crisis on the fair presentation of financial statements and on the workload for both preparation and auditing of annual financial statements.

Table 4 - Managers' perception about the impact of financial crisis on the fair presentation of financial statements and on the workload for both preparation and auditing of annual financial statements

	Total disagreement (1)	*Partial disagreement (2)*	*Neither agree or disagree (3)*	*Partial agreement (4)*	*Total agreement (5)*	**TOTAL**	**Average frequency**	**Standard deviation**	**Rank**
Workload for preparation of financial reports	9	21	39	29	31	129	**3,40**	**1,22**	**3**
%	*6,98%*	*16,28%*	*30,23%*	*22,48%*	*24,03 %*	*100,00%*			
Fair presentation of financial statements	2	18	23	43	43	129	**3,83**	**1,09**	**1**
%	*1,55%*	*13,95%*	*17,83%*	*33,33%*	*33,33 %*	*100,00%*			
Workload of management during audit engagements	3	20	36	32	38	129	**3,64**	**1,13**	**2**
%	*2,33%*	*15,50%*	*27,91%*	*24,81%*	*29,46 %*	*100,00%*			
Workload of audit team	15	29	38	23	24	129	**3,09**	**1,27**	**4**

during audit engagements									
%	*11,63%*	*22,48%*	*29,46%*	*17,83%*	*18,60 %*	*100,00%*			

Source: own projection

According to managers, the current financial crisis has most influenced the fair presentation of financial statements (average frequency of 3.83) but also the workload of management and financial-accounting department during audit engagements (average frequency of 3.64).

This result confirms once again the previously exposed ides that managers are generally unhappy that auditors request too many information on the activity to be audited (as shown above). We note that the values obtained for the other effects are similar: 3.40, respectively 3.09, with plus or minus deviations between 1.09 and 1.27.

Table 5 - Auditors' perception about the impact of financial crisis on the fair presentation of financial statements and on the workload for both preparation and auditing of annual financial statements

	Total disagreement (1)	*Partial disagreement (2)*	*Neither agree or disagree (3)*	*Partial agreement (4)*	*Total agreement (5)*	**TOTAL**	**Average frequency**	**Standard deviation**	**Rank**
Workload for preparation of financial reports	15	33	79	28	8	163	**2,88**	**0,96**	**3**
%	*9,20%*	*20,25%*	*48,47%*	*17,18%*	*4,91%*	*100,00%*			
Fair presentation of financial statements	6	4	35	76	42	163	**3,88**	**0,95**	**2**
%	*3,68%*	*2,45%*	*21,47%*	*46,63%*	*25,77%*	*100,00%*			
Workload of management during audit engagements	25	63	49	20	6	163	**2,50**	**1,01**	**4**

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%	*15,34%*	*38,65%*	*30,06%*	*12,27%*	*3,68%*	*100,00%*			
Workload of audit team during audit engagements	2	4	24	71	62	163	**4,15**	**0,85**	**1**
%	*1,23%*	*2,45%*	*14,72%*	*43,56%*	*38,04%*	*100,00%*			

Source: own projection

On the other hand, auditors consider that the unstable socio-economic environment especially has had an impact on the workload during audit engagements (average frequency of 4.15), respectively the time allocated to audit engagements increased and they act with greater prudence and thoroughness.

This result can also be correlated with the fact that most opinions issued by auditors are now modified to the detriment of those unqualified, which had a much higher weight in the total reports issued before the crisis (as presented above – questions 9 and 10 – auditors' questionnaire).

We note a partial disagreement in auditors' perception about the effect of financial crisis on the workload of management and financial-accounting department during audit engagements (only 2.50).

Table 6 - Perception gaps of managers and auditors about the impact of financial crisis on the fair presentation of financial statements and on the workload for both preparation and auditing of annual financial statements

	Managers			**Financial Auditors**		
	Average Frequency	**Standard Deviation**	**Rank**	**Average Frequency**	**Standard Deviation**	**Rank**
Workload for preparation of financial reports	3,40	1,22	**3**	2,88	0,96	**3**
Fair presentation of financial statements	3,83	1,09	**1**	3,88	0,95	**2**
Workload of management during audit engagements	3,64	1,13	**2**	2,50	1,01	**4**
Workload of audit team during audit engagements	3,09	1,27	**4**	4,15	0,85	**1**

Source: own projection

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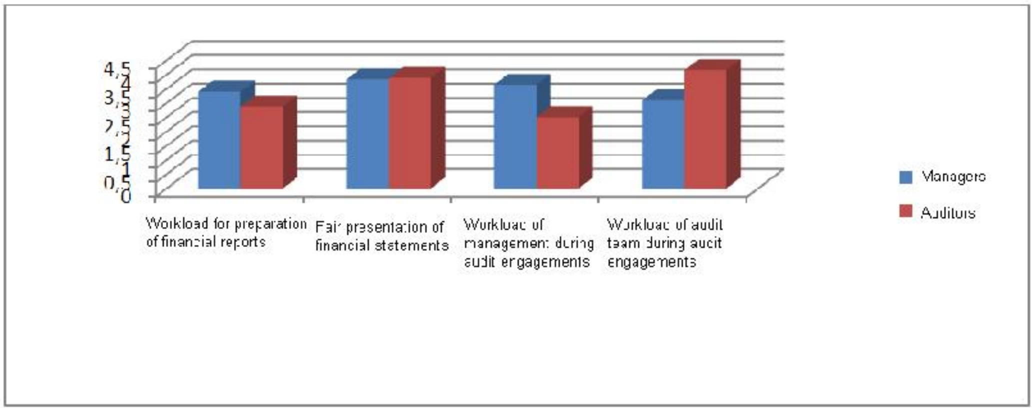
The chart below also shows this large gap between perception of auditors and managers about efforts of each of the two groups during audit engagements.

Chart 11 - Top of financial crisis effects on the fair presentation of financial statements and on the workload for both preparation and auditing of annual financial statements



Source: own projection

VI. Interpretation of results and conclusions – assumption validation

The conclusions drawn from the investigation are as following:

C_A: The financial crisis had a significant impact on the *turnover* of audit companies in Romania by reducing it in 2012 (year characterised by the effects of an unstable socio-economic environment) compared to 2008 (before the actual impact of the crisis effects).
C_B: The financial crisis has had an impact on the *average level of audit fees* collected by audit companies, by decreasing them in 2012 compared to 2008. Auditors were under pressure from clients to reduce their fees.
C_C: According to managers, the main difficulty faced during audit engagements in the last 5 years of financial crisis relates to *auditors' request for higher fees*. Also, dissatisfaction is related to the *large volume of information requested by auditors on the activity to be audited.* On the other hand, auditors seem to be dissatisfied with the *requests of audited companies for lower fees*, and they consider that *access to information on the activity to be audited* was not easy.

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C_D: According to managers, *the number of unqualified opinions declined significantly* from 2008 to 2012, while the *number of qualified opinions has grown remarkably*.
C_E: Amid financial crisis, auditors have taken some measures (both literally and figuratively), being *more reluctant to issue audit reports with „clean" opinions*, and the *weight of unqualified opinions decreased significantly*. Therefore, most unqualified opinions in total reports issued for financial year 2008 have been replaced by qualified opinions, and the *number of adverse opinions and cases of impossibility to issue an opinion has slightly increased*.
C_F: Both managers and auditors consider that the *current financial crisis had a greater impact on audit engagements than the adoption of IFRS*.
C_G: According to managers, the current crisis mostly influenced the *fair presentation of financial statements,* but also the *workload of management and financial-accounting department during audit engagements*, while auditors consider that the unstable socio-economic environment has had an impact especially on the *their workload during audit engagements*.

Based on the performed analysis, we noted that indeed ***financial crisis has had an impact on the activity of Romanian financial auditors*** and we can state that **assumption H is validated.**

Most of the study's results are hardly surprising, just confirming the assumption we started from. On the other hand, in our opinion, the article contributes to an increased transparency of the activity of Romanian active financial auditors. We believe that the used statistical instruments, but also the context in which this study was conducted provides credibility to our research and therefore, to the obtained results.

VII. Final conclusions and personal contributions

Our scientific approach started from a question on how external audits and audit reports are and should be regarded in view of the current sensitive socio-economic context. Although the original question seemed simple at first sight, during our research we noted the magnitude of the context, factors, differences and opinions that influence but also result from this activity.

Our research on *„The impact of financial crisis on the financial audit activity in Romania"* took into consideration the more intense concerns in the current economic context for obtaining relevant and „insuring" information on the quality of financial-accounting information provided by various companies' financial statements.

In a world where the concept of globalization tends to become obsolete, where dynamism and complexity of financial operations reached levels that were difficult to anticipate, facing more often in recent years the effects of economic decisions influenced by a number of professional and ethical factors, financial audit, by means of the audit report, can and should become again one of the main pillars that underspin decision-making.

Unfortunately, in recent years, we face a continuous degradation of audit image and consequently of the financial auditors, due to the wave of scandals and bankruptcies of companies and financial institutions, where auditors have contributed more or less. All these have led to intensified efforts of audit professional bodies and regulators for analysing the causes of these phenomena in order to identify and impose a number of measures to restore this lack of credibility that is increasingly stronger in the results of auditors' work.

In our opinion, financial audit progressed and improved in line with the economic development, in response to the challenges of the society. It progressed historically, being present in some form in all periods in terms of concept and especially in terms of goals. Therefore, we believe that auditors and audit companies should not overlook the social importance of financial audit in current days, its position obtained after hundreds of years of efforts and eventually to extend its responsibilities, to seek new methods or procedures compatible with current needs that would support their work.

The idea of this article is that the *value of an audit should be tested permanently against the requirements of users and society*. *Accounting profession must build a solid case for the benefits that audits bring to business, economy and society*. Audit market is very sensitive, thus accurate perception of stakeholders of auditors' activity is essential.

The debate focused mainly on the fact that the *current crisis was generated not only by corporate blunders, but also by mistakes of governments and their budgetary policies*. In this context, we believe that *statutory audit could play a more active role in consolidating the global economic environment if it would be more involved in the audit of public institutions, including financial and budgetary policies*.

Based on the performed analysis, we noted that indeed the *financial crisis has had an impact on the activity of financial auditors in Romania.* Thus, based on the research performed, we concluded that *audit must evolve and expand in order to add more value for users*. Especially for listed companies and more than ever in times of crisis, audit must be more than an opinion on the historical financial statements. Auditors should be involved in aspects such as: *corporate governance effectiveness*, *assumptions underlying the business model of an organisation and its risk management*.

In our opinion, it is necessary for both the profession and the society as a whole to reach a reasonable balance between the degree of responsibility and accountability that an auditor should assume related to the fair presentation of financial statements and audit costs for the society.

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