Assessing methods for the quality of financial and accounting information

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Abstract: *Accounting is a logical knowledge tool based on a system of rules that thinking must follow in order to achieve goals. This objective generally takes into account the construction of the true image of reality, using the accounting principles that influence the quality of accounting information. This study highlights the assessing methods for the quality of accounting information. The analysis shows that there are certain methods that are used to measure and assess the quality and usefulness of accounting information to determine the extent to which the financial statements match each of the qualitative characteristics.*

Keywords: *accounting information quality, measurement models, financial situations, accounting principles*

JEL Classification: *M41*

Introduction

This work is aimed at highlighting the methods for assessing the quality of financial accounting information. As a main research technique we used the process of reviewing the literature, in order to identify the current state of knowledge, the existing needs, as well as the future research trends.

The qualitative characteristics of financial accounting information are configured in a hierarchy that links the objectives of financial reporting to the requirements of financial reporting and the requirements existing in the standards. Useful information is delimited by useless information for presentation in the financial statements.

The qualitative characteristics of financial accounting information are ranked, and an important position is occupied by relevance and credibility. They are considered the main attributes and high utility of accounting information.

However, the secondary characteristics are not to be neglected, they are comparability and intelligibility. At the next level in this hierarchy, we find the accounting principles.

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Basically, these qualitative characteristics provide the framework for development and action for accounting principles. Accounting principles on the other hand provides a framework for action, for accounting rules and regulations.

The methodology for configuring the information is an approach to meet the need for proximity between those who draw up the information and those who use it. Items included in the financial statements of an entity shall be consistent with accounting principles. Accounting principles contain a set of rules of economic conduct extending the notion of valuation from goods and financial relationships to potential assessment, performance evaluation, and perspective evaluation.

The going concern principle assumes that the entity continues its business normally for the foreseeable future.

The prudence principle does not allow the overvaluation of assets and incomes, respectively the undervaluation of liabilities and expenses, taking into account the depreciations, risks and possible losses generated by the performance of the activity of the current or previous year.

According to the principle of independence of the year, this is ensured by observing the techniques of "delimitation in time" of events, commitments, incomes, expenses, obligations and, implicitly, maturities. The principle of the separate valuation of assets and liabilities is the determination of the balance sheet position of each item, be it of an asset or a liability.

The principle of intangibles expresses the correlation between the opening balance sheet and the closing balance sheet, except for the corrections required by the application of I.A.S. 8. The principle of non-compensation emphasizes that the values of the active elements cannot be compensated with the values of the passive elements, respectively the income with expenses, except for the compensations between assets and liabilities admitted by the International Accounting Standards.

According to the principle of economic prevalence over legal, the information presented in the financial statements must reflect the economic reality of events and transactions, not only their legal form.

The materiality principle underlines that any item that has significant value must be presented separately in the financial statements. Elements with insignificant values of the same nature or similar functions must be summed up and they do not need to be presented separately.

The "accrual" principle of accounting emphasizes the need for transactions and events to be recorded in the accounts when they appear and not when the amounts are paid or collected.

The presented paper is structured in three chapters. The next section is represented by the review of the literature. The second section presents various methods of measuring the quality of accounting information. The last section concludes the paper.

1. The importance of accounting principles for a company's activity

Compliance with accounting principles is the recipe of the true and fair view (Ciocan, 2021). Accounting principles make a primary contribution to achieving the objective of financial reporting. The true image is that concept, which imposed on the European economic entities the approach of accounting in the light of fundamental accounting principles.

However, the true and fair view should not be confused with accounting principles and rules. Some scholars argue that the true image is a goal to achieve, not a principle, aimed at accounting truth. In other words, the accounting information, collected from the primary documents, must be processed in accordance with the provisions of the accounting principles and rules, in order to present real and correct information.

Accounting principles are defined as a set of rules and basic notions of science accounting, presented from a theoretical point of view. However, if we carry out an analysis of the accounting principles in different countries, we see that all countries are obliged to comply with certain general rules, referred to differently from country to country, and their essence is practically the same.

Principles traditionally occupy a more prominent place in Anglo-Saxon accounting than in the continent, but with the development of international accounting, their role is growing in continental Europe (Lazari, 2018). The continuity of the entity's activity has been and is intensely researched both by the academic environment and professional bodies, as well as by the financial consulting entities (Hațegan, 2021).

It is presumed that an entity carries out a continuous activity for as long as possible. Given that its functioning depends on both internal and external factors, continuity can be affected to a considerable extent. The presentation of the companies' information in the financial statements is made by the management according to the principle of continuity of activity.

In a study regarding the evolution of entities and the risk of maintaining / developing a budding business, a specific link is pursued, in order to discover the internal reserves that must be exploited, in order to fulfill and respect the "principle of continuity", the essence of an economically efficient business (Stoian, 2015).

The presumption of business continuity depends on some criteria as follows: operating criteria and financial criteria. The entity's operating criterion suggests not violating the principle of continuity required by accounting rules. The financial criterion ensures business continuity.

A study explores rules- and principle-based accounting to measure the quality of financial reporting. It has been found that several standards based on principles such as the IFRS Financial Reporting Standard, which are applied by European firms listed on the stock exchange, offer more discretion about the management of earnings and their implications for accounting standards (Sundvik, 2018). The author notes that earnings management is largely a factor for decreasing the quality of reporting and that managers use their discretion on accounting options, reporting choices and real business decisions with the ultimate goal of influencing how events are reflected in different forms of revenue.

According to IASB a key prerequisite for quality in financial reporting is the adherence to the objective and the qualitative characteristics of financial reporting information. Qualitative characteristics are the attributes that make financial information useful and consist of relevance, faithful representation, comparability, verifiability, timeliness and understandability.

Another study identifies the key factors that influence and improve the quality of financial reports, as well as the factors that lead to poor quality. Results indicate that auditors perceive the qualitative characteristics of financial reporting information as important quality elements of financial reports (Tasios, 2012).

Auditors perceive all qualitative characteristics as very important quality elements of financial reports with higher perceived importance on faithful representation and comparability and lower to timeliness. This is consistent with the definition of financial reporting quality given by most of the respondents, who used the term “to faithfully represent the financial position” in their comments in non-mandatory field in which they were asked to give their own definition of financial reporting quality.

Financial reporting quality is a key prerequisite for the effective functioning of the economy. In order to fulfill their primary objective, which is to facilitate economic decision making without misleading or obfuscating the users, financial reports should meet certain qualitative characteristics. These characteristics are divided by IASB into two categories: fundamental and enhancing. Fundamental characteristics consist of relevance and faithful representation. Enhancing characteristics comprise of comparability, verifiability, timeliness and understandability.

Various methods have been used to assess the quality of financial reporting which can be categorized in four broad categories: accrual methods, value relevance models, specific elements of financial reports and methods that operationalize the qualitative characteristics.

Accrual methods and value relevance models focus on the earnings dimension of financial reporting. According to Folsom (2016), firm revenues are more informative and persistent and have a higher level of positive association with future cash flows on average when firm standards are based more on principles.

In the following, the results obtained by various authors who have tried to identify the existing relationships between the quality of accounting information and the options that companies have in various fields, such as in the field of investments, are presented.

Tsoncheva (2014) presents a sample methodology for measuring and assessing the quality and usefulness of accounting information to establish the extent to which financial statements match each of the qualitative characteristics, separately and in combination.

When constructing a measurement tool it is important to refer to the literature, which defines the quality of financial reporting with regard to the basic rights and the improvement of qualitative characteristics which are the foundation of usefulness, as it is defined in the conceptual framework.

The basic qualitative characteristics (i.e., relevance and faithful representation, understandability, and comparability) are among the most important ones and largely determine the contents of the financial reporting information. Raising the level of qualitative characteristics results in great improvements in the usefulness and the effectiveness of decision–making.

Overall assessment of the quality of financial reporting is essential as it can improve the quality of the economic decisions consumers make and improve market efficiency in general, thus reducing the price of capital for the business enterprises.

Carp (2016) develops the evaluation methods that predominantly introduce financial data into the analysis, the intelligence capacity which depends on the relevance of the informational output. The author looked at the impact of the quality of the reported financial information on the value size of the companies in terms of relevance, neutrality (non-alteration through manipulation) and persistence, as well as at the influence of these characteristics on the companies' market values. The study estimates the relevance, accurate representation of facts, economic phenomena, and the persistence of financial information.

The influence of these characteristics on the market value is also analyzed, while also involving non-financial factors in the debate, such as: the reputation of the auditor, the nature of the audit opinion or the specifics of the accounting rules applied.

In ensuring the quality of financial information, the role of the financial auditor is to express his opinion on the compliance of the statements with a financial reporting framework (Robu, 2016). On the basis of the mandate received, the auditor shall express a competent, objective and independent opinion on the quality of the information in the audited financial statements.

However, the audit opinion may be influenced by the quality of the financial audit engagement, supported by the requirements of competence, ethical and professional conduct that the auditor must take into account in the performance of his mandate. The author measured the influence of the auditor's rotation on the quality of the information in the financial statements (individual and consolidated) of the companies listed on the Bucharest Stock Exchange (BSE), with a direct impact on the investors' decisions. The study was conducted at the level of Romanian companies listed on BSE. The information in the audited financial statements was relevant. Relevance was assessed on the basis of the effects of the disclosure of information in the financial statements on the exchange rate under the influence of auditor rotation.

Another study examined the effect of the auditor's report and the size of the audit firm on the values of the relevance of the accounting information of companies listed on the Tehran Stock Exchange during the years 2008–2017. The author compared how financial market data and accounting data affect share prices and returns (Belesis, 2020).

Hribar (2014) investigates whether audit fees can be used to construct a summary measure of accounting quality. The measure assumes that auditors charge higher fees to firms with lower quality accounting. According to authors, when auditors perceive a client's accounting quality to be low, they should increase both audit hours and audit fees resulting in improved accounting quality. Zhai (2016) examined whether and how accounting information quality has an effect on corporate investment choices, based on the governance function of accounting information. This issue is very important to government, market participants, current and latent investors, and listed firms. The authors calculate the accrual quality. According to the authors, the higher the accounting information quality is, the higher the correlation and synchronicity of operating income growth between the listed firm and its industry. Moreover, high-quality accounting information serves an important governance role, which can supervise and push management to optimize capital investment choices.

The value of financial accounting is determined largely by its quality. The central concept of accounting quality is that some accounting information is better than other accounting information at communicating what it purports to communicate. For that reason, accounting quality is of great interest to participants in the financial reporting supply chain. For example, to a reporting entity, better accounting quality can translate into a lower cost of capital (Bruce, 2013).

Other authors have identified the measurement of the quality of financial accounting information as two types of dimensions: (1) decision usefulness and (2) stewardship (or accountability) based on the conceptual framework of the International Financial Reporting Standards.

Earnings quality as decision usefulness is measured as persistence and value-relevance, while earnings quality as stewardship (or accountability is measured as conservatism and accruals quality. Earnings quality means the firm's accounting performance and is a useful measure for assessing firm value. Yohan (2017) finds that the earnings quality of Korean firms is relatively lower than that of benchmark countries except for conservatism. The result of this study implies that Korean firms engage in earnings management in the presence of economic incentives, thereby reducing earnings quality.

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2. Methods of measuring the quality of accounting information

There are various methods of measuring the quality of accounting information in the literature: the questionnaire, the parsimonious model, the reflexive measurement model, the Pearson correlation test, the rational methodology, the measure of the risks, the Kormendi and Lipe model, the earnings management, the XGBoost method in the financial field reporting area - the model with fixed effects, timeliness, financial restatements, earnings quality, disclosure quality, audit delay, the use of fair value accounting, the auditor's report, data analysis, the Jones Model, the Mjones model, and the Stubben model.

According to a study on the link between the quality of accounting information and systematic risk factors, the quality of accounting information is an additional systematic risk factor that is different from other factors (Xuejing, 2018). The impact of accounting information quality on systematic risk is not only statistically significant but also economically meaningful. Systematic risk is significantly and negatively associated with ROA (return on assets) and firm focus, but positively related to firm size, market-to-book ratio, and firm leverage. The authors suggested that increases in accounting information quality cause systematic risk to decrease.

Another study examined the influence of top management support and effective leadership on the quality of financial accounting information system. Management support is an important component to information systems success. The top management is providing human resources, hardware, software, and funds needed to operate financial accounting information systems (Darma, 2018). The author used the reflective measurement model.

A study from 2019 deals with In order to be able to correctly assess the results of the study on the assessment of the quality of accounting information of entities in the third sector, non-profit organizations and the characteristics of Brazilian entities, and the results show that the moment of establishment of entities and their size positively influence the quality of accounting information (Ramos, 2019). The analysis was completed using the Pearson correlation test, aimed at the assessment of the relationship between variables such as assets, creation time, independent audit engagement, legal form and certification with the quality score of accounting information identified in the entities. According to the author, non-profit organizations and regulatory bodies need to evolve in the accounting information reporting process, as well as in the awareness of the importance of these reports for the decision-making process and public accountability. Therefore, the largest and most experienced organizations tend to have better quality of accounting information disclosed, which may be linked to the existence of more efficient controls, better knowledge of norms and experience on how to handle the accounting processes.

An important method of measuring the quality of financial accounting information is highlighted by Golochalova (2020) through rational methodology. The reliability of financial information is provided, by applying the IFRS Concept, which contains a description of the qualitative characteristics and their application. The presence in the IFRS Concept of qualitative characteristics, definitions of various notions, concepts, and other theoretical judgments, distinguish IFRS as a modern accounting methodology.

The IFRS Concept is used as a tool for the development of new international standards, changes or cancellation of existing standards, and as a guide in the preparation of national standards by particular countries. The high-quality information has many benefits to the users of accounting information, it is important to measure the risks, it is important to the practitioners and authorities, and it helps in the efficient assignment of the capital as it reduces the cost of capital.

According to Asmaa (2022), the quality of accounting information is measured with different methods, and some of them use the sequential properties in time series to measure the continuity of profits, the predictability of profits, and the profit changes. Other methods use the cash flow and the accounting accrual and others use the asymmetric recognition of loss and profits. Some methods use the unusual items of earnings and expenditures or what is called "the extraordinary items".

According to theoretical expectations, high-quality financial statements have many benefits to the users of accounting information (Piechocka-Kaluzna, 2021). The author used the XGBoost method of 'switch companies' – companies that transferred their accounting framework from the Polish Accounting Rules (PAR) to the International Financial Reporting Standards (IFRS). The method applied is widely used for classification, regression and ranking issues. The author studied the earning smoothing within the sample which assesses earning management for companies before (-pre) and after (-post) the transfer into IFRS.

According to Agienohuwa (2018), accounting quality is the ability of accounting measures to reflect the economic position and performance of a firm. The Mann-Whitney test was used to analyze the data. The author used a non-parametric test designed to check pre and post effects of any issue. In this case, the test was conducted to validate the hypotheses and determine the statistically significant difference in financial reporting quality between pre and post adoption of IFRS. Mann-Whitney test was used to analyze the data from all MDBs (Money Deposit Banks) in Nigeria. The result shows that there is statistically significant difference in the quality of financial reporting between pre and post IFRS adoption. Financial reporting quality increased in the post-IFRS adoption across the five qualitative features of relevance, faithful representation, comparability, understandability, and timeliness) examined.

The qualitative characteristics are an appropriate indicator of assessing and measuring the quality of accounting information. According to Alasbahi (2021), qualitative characteristics are considered a bridge between the objective of financial reporting and the concepts of recognition, disclosure, and measurement. The author noted that the characteristics of relevance, understandability, and comparability were accepted by most professional organizations in order to measure the quality of accounting information. Moreover, accounting information quality is a broad concept that does refer to the financial information included in financial reports that are useful for making decisions. Providing perfect methods for measuring the quality of accounting information is another global demand.

Dalkılıç (2021) developed a study for Turkey and used five different models to determine the quality of accounting information. First, Jones Model was used, where total accruals were evaluated as a function of changes in sales and tangible assets. The residuals obtained from the Jones model are considered as an indicator of accounting information quality. The second model used by the author is the Modified Jones Model, and the third is the earnings smoothing. The analysis shows that profits are smoothing more than cash flows, which is considered as an indicator of higher accounting information quality.

Other indicators of accounting information quality are earnings persistence and earnings predictability coefficients. The author shows that the accrual-based accounting information quality indicators (Jones and MJones) have a positive effect on the return on assets and price to earnings ratios of firms.

In the opinion of Albana (2021), the absence of a certain indicator in order to measure the quality of financial information, has led to different perceptions of users about what information to consider important. The study was carried out in Albania and was based on a structured questionnaire according to qualitative characteristics of financial statements defined by the conceptual framework of IFRS and FASB (Financial Accounting Standards Board) such as relevance and faithful representation of financial reporting, and also the comparability, verifiability, timeliness, and understandability. The author tried to find an answer to the following question: What is the attitude of the financial information users towards relevance, faithful representation, comparability, consistency, understandability, and reliability. The author shows that there is a strong correlation between the perception of users of reported financial statements about qualitative financial reporting and relevance as a fundamental qualitative characteristic. The quality of financial reporting has been considered a proxy for information risk. In the presence of poor financial reporting quality, uncertainty about a firm's future profitability is expected to be high, the analysts considering the firms with lower earnings quality as riskier. The hypotheses that have been raised were as follows:

- there is no significant relationship between the perception of users about quality of financial reporting and the qualitative characteristic of relevance;
- there is a significant relationship between the perception of users about quality of financial reporting and the qualitative characteristic of relevance.

El-Hewety (2019) investigates how the quality of accounting information measures the impact of investors' reaction to announcements of financial accounting restatements. According to the author, the restatement announcements are associated with increases in volatility and the magnitude of the change in volatility depends on the severity of the restatement. The quality of a firm's accounting information has an impact on the investor's view and interpretation of the negative economic news, leading to a smaller increase in investor uncertainty.

An (2017) measured the degree of conservatism as the relationship between accruals and negative cash flows.

Table 1. Analysis of methods for measuring the quality of financial information

No.	**Method**	**The title of the research**	**Author (s)**	**Year**	**Country**
1.	Measurement of the quality of financial information (i.e. relevance and faithful representation, understandability and comparability).	Measuring and assessing the quality and usefulness of accounting information	Tsoncheva, G.	2012	Bulgaria
2.	Comparability measurement method	Measuring accounting quality	Bruce, P.	2013	Republic of Ghana
3.	Measurement methods for accounting quality and audit fees	A new measure of accounting quality	Hribar P. et al	2014	USA
4.	Measure for capital investment choice as the correlation between the growth rate of operating income and that of the industry as a whole	Accounting information quality, governance efficiency and capital investment choice	Zhai, J. and Wang, Y.	2016	China
5.	Measure of earnings quality over time	Measuring earnings quality over time	An, Y.	2017	Republic of Korea
6.	Systematic risk measurement methods	Accounting information quality and systematic risk	Xuejing, X. and Shan, Y.	2018	USA
7.	The reflective measurement model	Measurement of the quality of financial accounting Information	Darma, J. et al	2018	Indonesia

No.	Method	The title of the research	Author (s)	Year	Country
8.	Mann-Whitney test for the pre and post effects	IFRS adoption and financial reporting quality: IASB qualitative characteristics approach	Agienohuwa, O.O. and Ilaboya, O.J.	2018	Nigeria
9.	Methods of measuring variables: assets, creation time, and independent audit engagement	Relationship between quality in accounting information and organizational characteristic of the third sector entities	Ramos, F.M. and Klann, R.C.	2019	Brazil
10.	Measure of earnings quality over time	The impact of the accounting quality and information risk on the time of earning announcement.	El-Hewety, A. and Ahmed, E.	2019	Egypt
11.	The method of comparing how financial market data and accounting data affect the prices and returns of shares	Financial market data versus accounting data: Which better explains stock returns?	Belesis, N. et al	2020	Iran
12.	Risk measurement method	Measurement of financial statements information in the context of harmonization of the accounting	Golochalova, I. and Tsurcanu, V.	2020	Republic of Moldova
13.	XGBoost method	Measuring the quality of financial statements after the conversion to IFRS, case of Poland	Piechocka-Kaluzna, A.	2021	Poland
14.	Assessing method for the quality of information using qualitative characteristics	Qualitative characteristics as a reliable tool for assessing the quality of accounting information: an overview study.	Alasbahi, A.H.M.A. and Ishwara P. I. P.	2021	India
15.	Jones Model, Modified Jones Model and Stubben model	The effect of Accountıng informatıon qualıty on firm performance and firm value: evidence from Turkey	Dalkılıç, E. et al	2021	Turkey
16.	Structured questionnaire	Qualitative characteristics of financial reporting: An	Albana, G.K. et al	2021	Albania

No.	Method	The title of the research	Author (s)	Year	Country
		evaluation according to the Albanian users' perception			
17.	The cash flow, the accounting accrual, and the asymmetric recognition of loss and profits	The methods of measuring the quality of accounting information: A comparative study.	Asmaa K. Al-Orfali, Eman A. Mal allah	2022	Iraq

Source: developed by the author

In the above-listed table several methods for measuring the quality of financial accounting information applied for the case of various countries and different periods were presented. To determine the methods used, the results obtained by the authors of seventeen papers from the literature, published in the period 2012-2022, were analyzed.

3. Conclusions

In this paper various methods of measuring the quality of accounting information were presented and discussed. These methods help in identifying the financial accounting information provided by the system accounting officer for the management of any economic entity. The compliance with accounting and tax rules is important for any business, having an impact on the decisions adopted by the management or by any other control body.

Accounting information must be accurate, homogeneous, verifiable, useful, and timely. Also, it must be presented in accordance with the legal and economic basis, and regularly, so that it can be used in the decision-making process.

Future research could consider a focus on European Union countries, to identify the used methods. Also, this topic could be investigated by employing a questionnaire-based analysis.

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