



## Investigation of impact of public ownership on the quality of benefit in the accepted firms of Tehran's securities and exchange organization

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### ABSTRACT

The quality of benefit depends on being useful in decision making as being related, reliability, comparability and stability. According to David Aboudi, quality of benefit, is a part of accounting profit that is sensitive about need and insight of management. Dilot & Tash argue that several factors such as liquidity, accurate measurement and variable estimates are used in evaluating of quality of benefit. This evaluation helps the user's judgment about trusting to the current income and future perspective. Using accounting principles in most of the firms leads to providing reported benefit by a range of quality of benefit instead of specified ridging. It means that the quality of benefit directly is related to cash flow and amount of current estimation of it and subjective benefit will be at least as much as benefit has low estimation or high quality, as a result it will have high quality. In addition, the best quality is obtained when the benefit has the high liquidity and low estimation. It should be noted that all criteria should be considered not only one special criterion.

### Keyword:

general ownership, quality of benefit, benefit management, conservatism in accounting, accruals

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## INTRODUCTION

Financial reports are one of the most important outputs of accounting system that one of its most significant goals is providing necessary information for evaluation of operation, firms' profitability and predicting future cash flows. Net profit is one of the accounting items that is being presented in the profit and lost statement.

This profit is calculated in accrual and under the influence of accounting procedures that are chosen by management. Accepted principals of accounting make it possible for managers to choose various ways of accounting and as a result, management (is able to / has authority of) scheduling identification of incomes and costs and determination of their amount as well. Management may overestimate the firm's benefit for reasons such as job security, receiving bonus, increase the firm's etc., in order to present desired image of operation of firm. On the other hand, management may handle the profit to reach to pre-determined goals. As a result of this, accruals are increased and difference between operation profit and cash that is derived of operation, will be grown and reported profit will have a low quality even though it is originated of actual operation of economical units and cannot be effective about economical decision making, so according to researchers and investors, the issue of quality of profit is so important (so the issue of quality of profit is so important in the opinion of researchers and investors). The quality of accounting information is affected by various factors that most of them are originated of demand of such an information in order to use in the contractual contracts and managers' motivation and opportunity to managing reported values. As the quality of profit has multiple dimensions, demand for quality of accounting information for contractual goals and motivation of managers to adjusting reported profit as well, are effected by whether the firm has general ownership or not.

In this research, some characteristics are investigated that are linked to quality of profit by former researches. The impact of general ownership on the quality of accounting values, was investigated by previous studies limitedly.

### Theoretical

In the second half of the twentieth century, in the large number of firms, general investors became one of the most important tools of capital market

and for instance, the general shareholders were increased from 6.1% of firms' total ownership in 1950 to more than 50% in 2002, in America. Assets that are available for general shareholders in the other financial markets are grown as well. For example, total financial capitals of organization of European Union is grown to more than 150%, between 1992 and 1999, although the role of general investors in countries with newfound capital markets is not so significant. But privatization is started to effecting on units' financial capital and so will impress on capital market of these economics. The suitable role of general shareholders in each economy is a controversial issue. Shareholders as the owners of firms has specified rights such as choosing board of directors whom have responsibility of monitoring firms' managers and their operation, as the representative of shareholders. Shareholders just like general investors can sell their shares if they are not satisfied with the function of board of directors in the firm or express their dissatisfaction and maintain their own shares and in return, in most of situations, because the percent of general shareholders' shares is more, the salability of their shares is less. As a result, the sufficient supervision should be about the managers' function, in return, this is not feasible for micro shareholders because of high cost of monitoring. (Tabatabaie et al.- 2011)

Those who use financial reports in their investment and contracts resolutions are interested in earnings quality. Additionally, the codifiers believe that the quality standard of the financial reports indirectly show how well the reports have been done. The reported earnings and the formula are usually used in the legal contracts of salary, prize and borrowing arrangements. Low-earnings based contracts would cause losing the money. For example, too much earning is used to evaluate the management performance and will lead to too many perks for the manager. Similarly, too much benefit may hide the sudden bankrupt of the company which can end up with wrong credit by credit-givers. In investment point of view, low earnings quality is not desirable. Surely, the low earnings quality which is not efficient as well as the wrong designation of capital will both lead to decrease in the economic growth. Also it will create a distortion of sources of plans of factual feedback and unreal ones which will reduce the

economic growth as well. Finally, the codifiers after seeking for the feedback of accounting standards to see if they are efficient enough, final reports such as the earnings reports are will be looked at closely. The criteria of efficiency evaluation are based on FASB and also the report of honest earnings rate of the Hicks can be considered as a criterion. As a result, the conceptual research model is shown below:



### History of research

#### Internal research

Noroush and Ebrahimi(2005) did a study on relation between combining of shareholders with symmetry of information and profitability of performance criteria. They aimed to show the role of public investment in reducing the lack of symmetry of information in Tehran stock. The research showed that the companies with more public ownership have been reported more information about the future earnings than the companies with less public ownership. Noroush and Ebrahimi Kordler(2005), did a study on the relation between public shareholders and symmetry of information in Tehran securities stock. The research shows that share prices have more of the future earnings information in companies with more public ownership in comparison to companies with less public ownership. They thought that the result depends on how professional the public shareholders are. Due to this reason, larger part of the information of future earnings must be gained out of share prices of companies with more public ownership. They came to the result that there is more lack of symmetry of information in companies with higher level of public investors compared with the companies with lower level. The relation between earnings and returns is usually influenced by other factors which need to be controlled. In this paper, there are two control variables: Representation and earnings quality. Representation variables are: size of company and lever (debt). In this article, size of the company is going to be evaluated by

sum of properties logarithm and the lever by the relation of long-term debt of the whole properties is going to be evaluated. Hasas Yegani and his colleagues (1999) did a research on public investors' supervising role to see if public ownership has effect on value of the company. They came to the conclusion that there is direct relation between the level of public investors and value of the company.

#### Foreign Researches

Almaz and his colleagues (2005): investigation of the relation between active public investors and control cost payment. In their paper, it is suggested that public investors play an important role in management control. Public investors that are not in business with the enterprises have a big role in ownership structure, organizing, supervising the activities and managerial decision-makings. General investors, who don't have direct business cooperation with companies, play a key role in organizing supervising and decisions are made by managers. Smith(2006), did a research about how general share-holders affect the company to focus better on its performance and reached the conclusion that supervising done by general investors can result in better focus on companies performance and less focus on opportunistic behaviors. Novisi and Nicker(2006), conducted a research about relation between public ownership and company's value and result shows that general investors have a higher motivation on supervising on management, hence their presence has a direct impact on the company's value, but on the other hand in higher levels general investors ownership can lead the board of directors to make useful decisions. Cornt and his colleagues(2007), did a survey about relations between general investors and company's performance. The result was, there is a key relation between company's financial feedback and the percentage of its shareholders. Chen and his colleagues (2007), did a survey about the link between control and general investors and by using classification realized that general investors help the company to make better decisions, but it's not the same for all investors and works for general investors who don't have direct business relation with the company. Mayeg (2008), believes that whether the changes general investors can make in the company are based on the amount of investment they have made. He concluded that if the percentage of general

shareholders' ownership were higher, the possibility of selling shares would be lower and as a result they need to keep their shares for a longer period, and at this moment there is a higher motivation to supervise company's management. Although, if general investors have lower share in the company and company performance is low, they can exchange their shares to cash and as a result management supervision goes lower.

Zhoe and his colleagues (2012), carried out a survey on effects of ownership over profits quality in companies which are in the stock market in China. To these reason, the date of 1438 companies in Shen Zhen stock market and Shanghai from 1999 to 2006 is gathered and collected them, the study their findings which show that albeit almost 75 % of all companies in stock market in China are one with the state-run system and ownership and they are bigger in size and more profitable, private companies are much more profitable and act more like market mechanisms. Results show that the companies with foreign ownership have the highest rate of profit and companies with employment ownership the lowest among ownership categories.

#### Research hypothesis:

Major hypothesis: companies include public ownership have more stable profits over companies don't. Companies with public ownership are more committed than companies without it. Companies with public ownership make few mistakes in their process than companies without it. Companies include public ownership are more conservative than companies do not.

#### Research approach:

This research, according to its goal, is a kind of practical research. Conducting a research in the comparison framework is done in an inductive manner. As the basis of the theoretical and the background of research through library studying has been gathered to confirm or reject theories.

#### The approach which has been used in this research:

To evaluate the quality of profit through the equation has shown (Phama 2004) we use this:

$$OI_{(i,t+1)} = q_0 + q_1 * CF_{it} + q_2 * ACCR_{it} + q_3 * Private_{it} + q_4 * Private_{it} * CF_{it} + q_5 * Private_{it} * ACCR_{it} + \epsilon_{it}$$

OI: Gross

ACCR: net profit subtracted annual operational cash flow over all assets in the beginning of the year.

CF: Operational cash profit achieved by equation (OI - ACCR).

Private: the standard for evaluating public ownership (in private companies it is 1 and otherwise it is 0).

To affect the extra variables on abovementioned regression, following controlled variables are used:

Leverage: the result of dividing the total of debt over the total of assets.

Size: is achieved through log (all assets)

Growth: achieved by

$$Growth_{it} = SALES_t / SALES_{(t-1)}$$

To measure the tolerance in this process, we use this (based on Lion and Visili 2005):

$$[(TCA)]_{(i,t)} = B_0 + B_1 \quad cfo_{(i,t-1)} + B_2 \quad cfo_{(i,t)} + B_3 \quad cfo_{(i,t+1)} + B_4 \quad [(\Delta Rev)]_{(i,t)} + B_5 \quad PPE_{(i,t)} + \epsilon_{(i,t)}$$

TCA: the total of current commitment which is obtained of current incomes except cash and current debts -  $\Delta CA$ .

$$(\Delta C - \Delta CL) = TCA$$

CFO: operational cash current

REV: the changes in incomes from the year t-1 to t

PPE: machines and facilities.

To measure and evaluate conservatism of accounting (Shivakmara 2005) the following model is used:

$$t-1) + a_2 \quad \cdot [(\Delta NI)]_{it} = a_0 + a_1 \quad [(\Delta DNI)]_{(i,t-1)} + a_2 \quad [(\Delta NI)]_{(i,t-1)} + a_3 \quad [(\Delta DNI)]_{(i,t-1)} + \epsilon_{(i,t-1)}$$

NIA: the changes in Gross

$\Delta DNI$ : the standard if NIA was negative last year, it equals zero and otherwise 1 (one).

To measure other items of commitment (Shivakmar 2005) used this:

$$[(ACC)]_{it} = a_0 + a_1 * [(DCFO)]_{it} + a_2 * [(CFO)]_{it} + a_3 * [(DCFO)]_{it} * [(CFO)]_{it} + \epsilon_{(i,t)}$$

ACC: the total commitment

CFO: current cash out of operations

DCFO: a virtual variable that if CFO is negative, equals one and otherwise is zero.

#### Evaluation and analyzing the result of theories test

According to what we reviewed in chapter 4, this chapter first we analyze major theories, and then we represent the whole result of the survey.

### Results of first major theory

Companies with public ownership, have more stable income than companies do not. The result achieved from testing this theory shows that connection factor of Pierson between dependent and independent variables is (0.171) that shows there is a positive connection. 42 percent of income stability is related to dependent and independent variables. According to the Sig which is less than 5 percent, in 95 percent of security level, H1 is assumed and in other words connection among variables are accepted. Additionally, the result of the test shows a liner and positive relation between public ownership and profit stability. Yaqi Shi (2009) in his study found out that there is a direct relation between public ownership and profit stability.

### Results of first side theory

Companies which have public ownership contain more stability of items of commitment than company that do not. The achieved results show the factor of connection between dependent and independent variables is 0.022 and shows a reverse relation between variables. Moreover, predefined and justified factor of 0.487 shows that 49 percent of changes in accruals are related to dependent variables.

Considering the fact that Sig is a test for less than 5 percent, 95 percent of H1 is usually accepted. In other words, integrity between words is confirmed. Additionally, the test of factors shows a reverse and meaningful relation. There is a reverse and meaningful relation between public ownership and accruals as the study of Butoson and Haris (2000) showed.

### Results of second side theory

Companies with public ownership have less tolerance than the other companies.

The results of test show that Pierson factor of integrity between the dependent variables and independent ones is 0.040 which shows a positive integrity between variables. Also the justified factor of 0.502 shows 50 percent of changes in dependent variables. Considering the fact that Sig is a test for less than 5 percent, 95 percent of H1 is usually accepted. Moreover, the result of test of factors shows a positive and meaningful relation while Tabtabae and his colleagues (2010) come to the conclusion that there is a positive and meaningful relation between public ownership and tolerance of estimated items.

### Results of third side theory

Companies with public ownership have more conservatism than the other companies.

The result of the test show that Pierson factor of integrity between the dependent and independent factor is 0.051 which shows a positive integrity between variables. Also, the justified factor of 0.624 shows 64 percent of changes in conservatism related to dependent variables. Considering the fact that Sig is a test for less than 5 percent, 95 percent of H1 is usually accepted. Moreover, the result of test of factors shows a positive and meaningful relation which Saeedi and his colleagues (2009) in their study found that there is a positive relation between public ownership and accounting conservatism.

### Conclusion

In conclusion of the study of theories to find out if there is a direct meaningful relation between dependent profit-quality variables and public ownership over the years of 2006 to 2012 can be stated that public ownership has a meaningful liner relation with quality of profit, reverse relation with accruals, positive and meaningful relation with tolerance of estimated items and finally a positive relation with accounting conservatism. This shows that the companies with more public ownership enjoy the benefit of more quality of profit as well as more stability in profit. Finally, we can come to the conclusion that investors by putting money into companies with more public ownership will result in more profit.

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