FINANCIAL THEORIES AND ACCOUNTING JUDGEMENTS REGARDING THE SYNTHETIC INFORMING

TEORII FINANCIARE ŞI JUDECĂŢI CONTABILE ÎN INFORMAREA DE SINTEZĂ

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Abstract: *The current work tries to brig into front the incidence of financial theories in the process of financial reporting. Thus, there are theories like: functional fixation theory, which supports the establishing of repetitive directions for analysis; anchor theory, which assumes that users of accounting information will select a specific available figure as a starting point for their analysis; efficient financial market theory, which indicates the measure of which the financial market incorporates historical data as well as privileged information into the market evolution.*

Key words: *financial theory, financial reporting, incidence, capitalization.*

INTRODUCTION

Accounting data is set at the border between accounting and financial analysis. Therefore, accounting theory, through the principles, norms, procedures, methods and specific instruments, is not sufficient for analysing and interpreting financial statements. For this purpose it is necessary to resort in addition to some theories specific to the capital markets, because after all, investors from the capital markets are the most important users in the new international understanding. The way through which the users of financial-accounting data utilise general financial statements is able to describe to great lengths the chance to succeed and prosper in a complex environment, where uncertainty exists regarding future events. Empirical studies, some of which are taken from psychology certify the tendency of individuals to simplify the economic reality through diverse processes, such as the constantly growing use of instruments for statistical and mathematical modelling of the economic processes.

MATERIALS AND METHODS

In order to piece together this study, multiple methods have been used concurrently as follows: comparative analysis, in theory as well in practice, synthesis, induction and deduction.

RESULTS AND DISCUTIONS

Two theories have been borrowed from the psychological literature, which have applicability in accounting as well, the functional fixation theory and the anchor theory. The functional fixation theory is frequently used in financial-accounting issues. Adriana Du escu has taken up the hard task, in an elaborate study[22], to summarize some aspects regarding the empirical studies that have been made in relation to the application of the functional fixation theory in the interpretation of accounting information on the capital market. She concluded that "this theory indicates that individuals utilize symbols, aggregates or surrogates when passing value judgments regarding the future, in such a way that their significance and relevance remain constant in time, without taking into consideration the modifications that took place in their consistency."

In other words, investors don't bother to interpret the accounting data; instead they rely only on a mechanical interpretation of the accounting numbers. A dissociation of the final accounting data from the methods through which they have been attained represents a huge mistake and implicitly the conclusions that follow regarding the cash flows of the business will be highly subjective.

If we add the effects of the signalling theory on top of the conclusion previously drawn we will discover that the asymmetry of information that the financial statement users are trying to eliminate is in turn being amplified. For example, each user must take into account the established tax accounting report when calculating the net worth. Two separate entities that are forced to adopt different tax treatments in relation to the calculation of

[22] Duţescu, Adriana., 2000, *Informaţia contabilă şi pieţele de capital*, Bucureşti, Editura Economică.

the profit tax, and that report the same accounting net income during one year, can report considerably different net worth the next year, only due to the change of the fiscal framework and not due to the effect of a more efficient use of economic resources. In such a situation, the accounting data becomes the investor's only source of information, leaving no room for alternative sources. This type of analysis of the financial-accounting data is consequent primarily of the capital market players' lack of knowledge regarding accounting reasoning.

The fixation theory's use can be justified only if the principle of perpetual methods is being followed or, when the accounting policy is modified the financial reporting will be done using both the initial method as well as the one being currently used. Although the functional fixation theory has in mind the reasoning of investors, in order to diminish as much as possible the bad effects of such an approach, the data producers represent the solution to get out of this hilarious situation.

They could report the financial data requested by the capital market in such a way that it would make possible a more profound understanding of economic conditions. Therefore, thorough an itemization of accounting data based on the informational needs of investors, the data producers should point out the black spots within the data and offer indications regarding the importance of the performance indicator's method of calculation.

The anchor theory is used alongside the functional fixation theory in order to simplify the complex situations that the data user is facing in regard to the data volume. In the same work, Adriana Du escu remarked that the anchor theory is based on the anchor method, also used in putting together macroeconomic policies.

The anchor theory presumes that the accounting data users designate, in advance, certain specific data as a starting point, which is relevant in their personal analysis and subsequently they go on to make adjustments in the forecasting process by collaborating the initial data with the new accounting data available. Therefore, the option for an anchor is directly dependent on the purpose of the analysis undertaken by the accounting data user. Thus a creditor can select as an anchor the level of debt at a certain point in time, while the stockholder may rather opt for an anchor that represents the dividend distribution rate.

By comparison to the functional fixation theory, the anchor theory is not as simplistic and superficial. The difficulty arises when the accounting data user chooses an anchor, a mission that, again, requires specialized knowledge. The goal is to pick the most relevant anchor in the context of each user's annual financial statement. In addition, in order to transpose the newly acquired information into high quality adjustments on the initial anchor, there must be a very competent data user with finesse of reasoning regarding future forecasts concerning the evolution of the economic entity, its market value, or any other relevant indicator.

The efficiency of using the anchor method resides for the most part in the assembly of knowledge possessed by the accounting data user and from his/her ability to integrate the additional data or the adjustments of forecasts through the use of superior statistical methods. It is important to notice that with this theory there is no monopoly of the annual financial statements as a source of information used by analysts, creditors and investors.

We find it is opportune to have a public debate on identifying "relevant" anchors, utilized on an international level in order to help those players of the "social game of accounting", which considers that a cost of education is far higher than the loss incurred due to the placing of investments based only on raw accounting data, many times faulty and distorted as a consequence of tweaking the accounting data or of it arriving too late.

In the case of the anchor theory we spoke of the forecasting adjustments based on new information that is timely acquired by the users of accounting data. Obviously, these adjustments are based on complex economic mechanisms, which characterize the good functioning of the economic system and, in particular, the stock market. Within such an economical resources allocation system, any new information is automatically integrated, generating a series of value variations on some of the selected "anchors."

There is one question being raised the moment when although the accounting data user acquires this information within due time, at low cost, adjustments considered in theory to be correct, differ significantly from the real values recorded in the future. The explanation for these differences comes from ignoring one essential hypothesis that is used when trying to

describe capital markets and more, and that is the efficient financial markets hypothesis.

It is obvious that the new financing scheme for the economy tends to concentrate more and more on obtaining the financing requirements off the capital market, as the stock market is the most powerful, competitive and efficient player of a capitalist economic system.

The efficient financial market theory has been outlined more and more in recent decades through numerous studies that have been conducted, starting with the empirical studies of Eugene Fama, who considers that "an efficient market" is one that has "the ability to adapt rapidly following the impact of the latest data available." The interest for this theme has been continued up until today, through the introduction of new, more refined methods of statistical analysis.

In his thorough work, professor Ion Stancu considers that "an efficient financial market is that particular market where the arbitration opportunities for the difference between the market value and the net present value (NPV) of the investment in buying a financial title are missing."[23]

Financial efficiency can be analysed from three separate perspectives:

- informational efficiency;
- organizational efficiency;
- operational efficiency.

By organizational efficiency we understand the allocation of resources in the Pareto sense. In other words, through allocating and organizational efficiency, we understand the speculative games played by the other participants on the capital market, with the intention to thwart the behaviour of the other participants on the capital market.

Operational efficiency refers to the degree of the participant's atomicity, the existence of risk free interest, the ensemble of mechanisms that are the basis for establishing equilibrium prices, and the absence of fiscal and transactional costs.

[23] Stancu I., 2008, *Finanţe - pieţe financiare şi gestiunea portofoliului*, Bucureşti, Editura Economică.

Informational efficiency is the most relevant in the context of this work. Through informational efficiency, the market ensures the reflection of all pertinent information, related to securities traded and market characteristics, in prices, without omissions or distortions.

In this context, where by informational efficiency we understand a cumulative integration of historical data, of publicly available information and privileged information, held only by stock holders and managers, in his study, Eugene Fama has established a pyramidal distinction regarding the concept of efficient financial markets, delimiting three types:

- weak type, in which the price of assets reflects all historical information, without the existence of the possibility for superior gains achieved by some of the market players based solely on this information;
- semi-strong type, in which the price of assets encapsulates not only historical data, but also all other available information regarding the assets as well;
- strong type, in which the price of assets reflect not only the information related to the historical evolution of current assets, but also privileged information, held by stock-holders and even more predominantly, managers.

Testing models for the efficient financial markets, by the use of informational entropy concepts, or by designing increasingly complex statistical tests holds no interest in the current work.

The importance of presenting these concepts has been given by the necessity to become aware, in the case of users, but more importantly in the case of accounting data producers. It has also been given by the necessity to report a clear picture, unbiased, because in an efficient financial market, accounting data receives an essential role in acquiring financial sources on the capital market.

Thus, the more accurate the financial statements will present the economic reality, regardless whether a certain situation might give the possibility for certain irrational investors to destroy the hypothesis of an optimal allocation of capitals, the more predictable can the market value of a certain entity's stocks be. Concurrently, the players on the capital market would be shielded from a series of costs involved with procuring the

necessary data required for future adjustments caused by financial and accounting tweaks.

An essential problem in perfecting the financial statements of business entities is represented by the existence of the phenomenon known as information asymmetry. This phenomenon starts from the social interactions between economical players, which are explained by the agency theory and, at the same time, from the governance policies used by the entity which are explained by the signalling theory.

It is obvious that economic players do not have free access to all the necessary data, but, at the same time the cost of acquiring this data is differentiated from one category of users to the next. In order to obtain a more careful analysis regarding the testing of the information asymmetry hypothesis, a new theory has been developed, the Agency theory, which tries to establish the socio-economical interactions that exist between economic players and the rights of each to information, together with the cost incurred in order to procure it.

In specialty literature different agency relationships can be distinguished:

- between managers and stock-holders;
- between creditors and stock-holders;
- between different categories of stock-holders;
- between creditors and managers.

In a simplified vision, oriented towards the finality of accounting data, the specialty literature has closely studied the phenomenon of informational asymmetry, the circumstances under which it takes place and the affected user categories, especially since this theme is proven to be of interest, through recent studies, like the ones made by Rutherford (2005), Johnson and Droege (2004) or Guilding (2003).

CONCLUSIONS

There are numerous means to perfect synthetic financial statements and it is important that the focus should not only go into the quantitative aspect of the published data, but into the qualitative aspect of the financial communication instruments and the financial communication methods used.

The supplying of forecasted data or the gradual giving up of accrual accounting, the preparation of reports meant to inform employees or the disclosure of the way added value indicators are being formed and how much each production factor contributes to the indicators are just a few ways to solve the problems of financial communication.

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