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Firms' Financial Reporting Transparency and the Rank of Financial Reporting Transparency

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Abstract
Financial crisis in global stock exchange especially September incident in 1997 and following Enron's financial disgrace and some European and American corporations at 2000 were caused that professional communities pay attention to information transparency issue in financial reporting process. Foreclosing public confidence from capital markets allows above countries to codify and amend rules that guarantee investors' confidence to commercial cycles and presented information by them. Sanction regulations such as Cadbury's reports (1992); Greenbury (1998) and Hampel (1998) in England, publication of Vinute's report (1996-1998) in France and financial security principle (2003); SOX in US (2002); KonTraG (1998); Berlinz (2000) and KapAEG (2005) in Germany show a new wave from attention to modifying strategic system frameworks that existed along increasing shareholders' right in stock exchange and enhancing external information quality (Estiger and Volf Gang 2008).
Keywords: Financial Reporting Transparency ,Rank of transparency, Exchange Firms

1. Introduction

It can almost be said that financial crisis in stock markets was mainly due to insufficient financial information transparency during current decade, in other hand; clarifying financial information by corporations has had more effect on investing method of investors. Many researches show that availability and the quality of firms' financial information are important factors that affect on investors' economical decisions (Young 2003). Studying the history of share market in Iran shows that Iran stock exchange has experienced financial crisis in sections and these crisis have been due to not presenting correct reports by corporations and proportionally disorienting rational relations between profitability and share price of firms. The problems of economic structure and government outbreak from monitoring position have been the main reasons of arising crisis during stock exchange activity period that has caused to foreclose the confidence of investors and their tendency to extracting capital from share market to other sections such as trading and investing on estate (GholamHossain Davani 2005).

2. Literature and Research Theoretical Framework

2.1. History

Bushman et al (2004) consider information transparency as a situation that information is broadly available, relative (concerned), dependable, possessing quality, extensive and timely. Following S&P definition, Aksu (2006) considers transparency as timeliness and the quality of financial functions disclosure and form operation. Chen et al (2007) studied the relationship between corporate governance and share liquidity on the basis of S&P ranking that is based on transparency rate and information disclosure. Theses researchers found that firms that have less information disclosure face with serious information asymmetry about information. According to Brown et al, the best definition of transparency in commercial area is as qualitative financial statements. Nillsen et al (2009) believe that information users know everything in every time and they can study each subject based on transparent information. Complete disclosure procedures associated with transparency in financial reporting can create safe conditions and increase confidence about supporting investors' benefits. Researches have also showed that voluntary disclosure has positive effect on firm performance and can affect on maintaining stakeholders and shareholders' benefits. In other words, the lack of information transparency and ambiguity in reporting may lead to suspiciousness and immoral behaviors along reducing firm's value (Madhani 2009). According to Kaufman and Vishwanath (1999), one can reach transparency through three ways:

1- Improving legal mechanism (or regulatory) related to more disclosure
2- Safety designing policies for restricting moral risk through more disclosure
3- Establishing legal institutions and policy-making for solving unavoidable problems of financial markets.

2.2. Transparency concept and definition

In culture, transparency is defined as: "openness of institutions, being overt of institutions, honesty and simple perceptibility." In this definition, openness of institutions means simple access to operation inside corporation and being overt of institutions means information transparency or obviousness.

There are other various definitions for transparency that due to emphasis on different concepts, one can distinguish them from each other in three categories as follow:

2.2.1. Definitions based on information stakeholders: Vishwanath and Kaufman (1999) and Kaufman (2002) have described transparency as "increasing timely and dependable flow of political, social and economical information that is available for all stakeholders", Vishwanath and Kaufman (1999) have also defined the lack of transparency as "intentional prevention of accessing to information, incorrect presentation of information and inability of market in obtaining confidence from adequacy, relativity and quality of presented information." Economic development and collaborative organization point of view is more broad and describes transparency as intercommunication between firms and other stakeholder groups."

2.2.2. Definitions based on responsiveness: transparency expert group in Brookings university has defined transparency as "openness and evolvement degree of institutions; i.e. the rate of supervising and evaluating performance of people inside corporation (such as managers) by people outside corporation (such as shareholders)." In Florini's definition of clearness, responsiveness or accountability has been more prominent. He has defined transparency as "disclosure information by corporations that is useful for evaluating their performance." From his view, transparency is a tool for facilitating the process of evaluating firms' performance. Emphasis on the right of accessing information and the ability to evaluate firms' performance has been more prominent with using this information in mentioned definitions. In fact, transparency has more relation to responsiveness and the reason for needing transparency is that market considers firms responsible for policies and their performance (Kaufman and Bellver 2005).

2.2.3. Transparency definition with emphasis on enforcing rules and regulations: universal commercial organization considers confidence from accessing to transparency in commercial international contracts that needs three substantive preconditions:

1) Information about rules, regulations and other procedures that has been published in public.
2) Stakeholder groups should be aware of rules and regulations and changes in them
3) Rules and regulations should be enforced as massive, impartially and reasonable.

The common aspect of these definitions is "availability of information" and "ability to communicate and existence of information receipt and transmission flow" (Tajvidi 2009).

2.3. The rank of financial reporting transparency

In substantive proclamation of accounting theories, relativity and dependability as two important qualitative financial information, have always been the important subjects of financial reporting literature and have been emphasized by professional institutions, legal authorities and financial information users. Timeliness means that information should be accessible to users as fast as possible. If the temporal interval between ending fiscal year and the date of publishing financial statements of commercial units are shorter, benefits and usefulness from annual audited financial statements of commercial units increase. The increase of temporal interval between ending fiscal year and the date of publishing financial statements enhances probability of information disclosure in favor of a group of users and in loss of others.

Other important qualitative characteristic has been described as dependability of financial information. Help to decision- making and maintain benefits of investors, trusters and other stakeholder groups as well as defined legal requirements in many countries have caused that auditing financial statements is planned and performed by a person except information provider. In spite of that advantage from audited financial statements is clear, accomplishment duration and completing auditing operation can affect on timeliness of presented financial statements and its relativity. Timely financial reporting depends on different factors. These factors can concern to auditor or auditing operation or properties of audited unit.

Bidli and Hilary and Rodregues (2009) stated that timeliness of financial statements is one of the most important components of firms' financial information quality, information timeliness can lead to better and more useful usage of information users that end product of accounting system transmits. In other words, timeliness of financial reporting can lead to more transparency of firms' financial information and as result more transparency of capital market that this subject can have more effect on capital and financial markets attractiveness.

Financial reporting with more quality with decreasing firm's investing in less or more boundaries helps increase its investing efficiency (Verdi 2006). The terms of "the quality" of accounting information disclosure and "transparency" of a disclosure system are used interchangeably and it is difficult to present an exact definition of "transparency" and "quality" that is accepted by all people (Kavsari 2000). Various words such as suitability, comprehensiveness, informant (instructive) and timeliness are used as representative of disclosure quality (Vallas and Mora 1994). Singhavi and Desay (1971) believe that quality refers to completeness, accuracy, precision and dependable characterizations. Ball et al (2000) and Kavsari (2000) interpret transparency as a mix of conservatism and timeliness. Bareth and Shipper (2008) claim that financial reporting transparency is a limitation (or realm) that reveals financial reports and economical affairs of a commercial unit so that it should be useable for its users. High transparency can decrease information asymmetry and incorrect selection and increase liquidity. Diamond (1985) concluded that investors' motivate for acquiring private information decrease with increasing disclosure of public information by firms. Generally there is more probability that firms with high disclosure present important public information and future information timely. It is expected that the quality of more disclosure reduces search motivate for private information. Recently, there have been attempts in stock organization about financial reporting transparency so that they categorize firms according to the rate of financial reporting clearness. Transparency rank in stock organization means regulating information that is available for stock organization and shareholders. More lower this number is, better it is. In fact transparency ranking is the same as transparency in financial reporting. Stock exchange categorizes them based on timely reporting and accuracy rate of predicts and reliability to firms' reports that shows it in transparency rank report. Each firm that its transparency rank is better faces with fewer ambiguities for investing; its EPS is more useable and has less risk. As a result, that firm has more value.

In order to defining transparency rank or financial information disclosure (timeliness and dependability), annual privileges (scores) of corporate disclosure quality will be used. Annual privileges of accepted corporations' disclosure quality have been calculated in Tehran stock exchange for periods of 3, 6, 9, 12 months and have been published by stock exchange organization for 1382 and onwards. Mentioned privileges calculated based on weight average of disclosed information dependable and timely criterions (Norosh and Husaini 2008). Financial reporting through firms' financial information transparency disclosure can decrease information asymmetry and cause optimal allocation of sources (correct selection instead of incorrect option) and firm's performance efficiency (management attempt for maintaining shareholders' benefits instead of moral risk or less function) (Kurdistani and Alavi 2010). The findings of various researches such as Betti et al (2007); Bidell and Hilary (2006 and 2007); Bidell et al (2009); Fransis et al (2005) and Verdi (2006) indicate that increasing financial reporting quality by reducing information asymmetry among managers with investors and loaners decreases moral risk and incorrect selection and leads to reduce management costs and finally decrease risk and expenses of firm's funding and financial reporting clearness. With interfering these factors, the probability of investing efficiency i.e. losing investing opportunities in projects with positive current value (investing fewer than limitation) or investing in projects with negative current value (investing more than limitation) decreases.

It should be noted that the privilege of publishers' informatics has been calculated based on their informatics situation from perspective of dependability and timeliness of information transmission. Studying the criterion of information timeliness is done based on transmitting information by corporation (including predicting the income of each share, audited midterm financial statements of 3, 6 and 9 months, auditor's notion about predicting income of each primary and 6-month share, end year unaudited financial statements, end year audited financial statements and scheduling shareholders' profit payment) in defined sections in information disclosure instruction and considering the number of delayed days due to instruction appointed time. Dependable criterion is evaluated due to the rate of changes and fluctuations in transmission forecasts and the difference between forecast and audited real performance. The following table shows transparency rank of few accepted firms in Tehran stock exchange. Firms that their transparency privilege is above 50, we consider transparency rank as 1 and firms that their transparency privilege is less than 50, its transparency rank are 0.

Table 1: financial reporting transparency rank of firms

Corporation name	Report year	Transparency privilege or financial information disclosure	Virtual variable of transparency rank
Iran Transfo	2014	66	1
Iran Khodro	2014	13	0
Iran Aluminium-Iralko	2014	56	1
Iran Behnoush	2014	61	1
Pars Khazar	2014	43	0
Pars Daroo	2014	70	1
Esfahan Petrochemical	2014	49	0
Iran Information - Processing	2014	86	1
Iran Radiator	2014	68	1
Tehran Cement	2014	62	1
Iran car fragments	2014	47	0
Iran Carburetor	2014	61	1
Esfahan tile	2014	86	1
Iran Carbon	2014	74	1
Iran Combain-making	2014	44	0
Bahman Group	2014	87	1
Butan Industrial Group	2014	88.59	1
Pak Dairy	2014	62	1
Iran brake lining	2014	86	1
Pars furniture	2014	45	0
Iran pipe and car-making	2014	69	1
Bafegh Mines	2014	57	1
Behran petroleum	2014	55	1
Pars Petroleum	2014	46	0
Motor Force	2014	69	1

3. Clarifying and financial information disclosure criterions

Transparency is increasing dependable and timely flow of political, social, financial and economical information that is available to all stakeholders (Vishwanath and Kaufman 2001). Vishwanath and Kaufman (1999) have also defined the lack of transparency as "intentional prevention of accessing to information, incorrect information presentation or market inability in obtaining confidence from relative adequacy and presented information quality. One of the researches defines clarifying as: eliminating latency and mysticalness and latency is attempt for hindering some behaviors and activities so that special group or people benefit from this cover (Hsiu 2006). Vishwanath and Kaufman (2001) have presented a model for measuring financial information disclosure. They addressed three criterions for clarifying information:

1) Availability or accessibility of information
2) Relativity
3) Quality and being reliable

Accessibility pays attention to corporate communication means for presenting financial information. A limitation that exists in measuring this criterion is the lack of information users' knowledge or training about how to use and analyze information. The second criterion is difficult because of defining suitable information. The third criterion is studying quality and reliability and refers to this component that published financial information should be effective, transparent and simple. This information should be according to accounting accepted principles.

Measuring criterions in standard and pourz (S&P) are divided in five categories that include: clarifying in ownership structure, investors' relations, financial clearness, information disclosure and directorate structure (Chiang 2005).

Due to these criterions, transparency includes investor's confidence to firms' financial proclamations in capital market. These five criterions are studied in three dimensions in this research:

1) **Ownership structure and investors' relations:** include identifying ownership structure and shareholders' combination during investing in a corporation or firm main decision-making especially identifying principal shareholders. This variable is measured based on enough information from

investors' structure especially main shareholders in assembly meeting, corporate policy and firm proclamation (Chiang 2005).

2) **Financial information disclosure**: includes existence of enough information and timeliness about firm activities (Chiang 2005).
3) **Directorate structure clearness**: Directorate structure transparency is the sum of clarifying criterions of directorate structure in a corporate that is measured based on integration of most directorate members, their experiences and proficiency. The investor's experience is amounts of years that the investor has been active as accepted firms' shareholder and owner in stock exchange and is measured based on length of profit receipt (Hsiu 2006).

4. Reporting transparency nature in financial texts

Transparency means accessing to relative and dependable information about periodical performance, financial situation, investing opportunities, corporate strategy and subordinated firms' risk (Bushman and Smith 2003) but transparency is divided into three categories from more exact view:

1) Definitions based on information stakeholders
2) Definitions based on accountability
3) Transparency from aspects of law (Taheri 2009).

First category:

Vishwanath and Kaufman (1999) believe that transparency means increasing timely and dependable flow of economic, social and political information that is accessible to all stakeholders. The lack of transparency in information means prohibition from accessing to correct information or incorrect information presentation or market inability to obtain confidence towards adequacy and relativity of presented information quality.

Second category:

Florini (1999) considers transparency as information disclosure by corporations that is necessary for evaluating performance and performing duty. He believes that transparency is a tool for facilitating the process of evaluating firms' performance. Emphasis on accessible right to information with considering realm of both parties provider and user and possibility of evaluating firms' performance with using this information has been more prominent in Florini's definitions and involves more accountability view (Tajvidi 2010). In fact, transparency has more relation with responsiveness and the reason of demand for transparency is that market considers firms responsible for their polities and performance.

Third category:

Third dimension of transparency is in field of legal responsibilities, in order to performing two above procedures by government and legislative authorities, firms are obligated to loyalty to disclosure requirements and clarifying information.

5. Transparency role in financial reporting

Based on financial reporting concept framework, financial information should have two aspects of relativity and dependable. However, information quality regarding to transparency is timely and suitable from view of information disclosure (Madhani 2009). Disclosure means information pervasion, but accountants' response to disclosure isn't interesting. Today, information disclosure isn't limited to financial information in financial reporting framework; firms disclose some nonfinancial information with the aim of affecting on users' decisions. Transparency is one of the effective factors on corporate attractiveness for investors and one of the main elements in corporate strategic systems framework. Transparency rate depends on management power and tendency for correcting informant discriminations for market participants. Capital markets will progress through establishing a transparent information environment. Financial information transparency has critical role in this environment. Firms that are disabled in realizing transparency standards have more risk that involves the credit of their managers. These firms will face with decreasing shareholders and investors confidence that will lead to capital market loss and reducing corporate credit place (locality) and liquidity in market. On the other hand, Madhani (2009) believes that there are significance benefits in voluntary disclosure for creating a transparent system. Information voluntary disclosure and transparent financial reporting helps firms in long-term to create competitive benefits. Bushman et al (2001) create an evaluation design for corporate transparency that was more aggregative in comparison with used transparency indexes in other studies. They measured transparency in three categories:

a) Corporate reporting quality measuring including volume, timeliness and firms' disclosure reliability (i.e. auditing quality).
b) Measuring volume for acquiring private information include analyzing and issuing investing mix tables and internal commercial activities
c) Measuring information quality
d) Public or private ownership of media (with the aim of informatics and attendance in public)

6. Notions relating to transparency and disclosing financial information

Among theories and presented ideas about financial information clearness, here we refer to two sign theories from Spans (1973) and rational action theory from Ajzen and Fishbein (1980).

6.1. Spans' sign theory

Spans' mark or sign theory has been propounded at 197. The concept of this theory is that there is skewed information in financial markets that can increase the risk for users of this information. One of the signs of financial information not clearing is the possibility of dealing and abusing information by people who have furtive information. Abusing information hasn't been a barrier to market efficiency rate, however it has increased the investors' concern in share market (Spans 1973). Vishwanath and Kaufman (2001) have designed a model for evaluating information disclosure. This model assesses information with considering three characterizations, information availability, relativity and dependability.

6.2. Rational action theory of Ajzen and Fishbein (1980)

Ajzen and Fishbein (1980) presented rational action theory with the aim of explaining human behavioral attentions. This theory studies human's physiological, psychological and behavioral system completely and states that humans often have purposeful behavior. In other words, they first investigate their decisions in their minds and then convert these decisions to action. Donaldson and Davis (1994) attributed rational action model to trading and commercial affairs. They stated that there is a positive relation between firm's performance and investor's behavior and financial reporting clearness. Uiddin and Gillet (2002) added some points to rational action theory in investing and trading.

Conclusion

The role of information transparency and firms' financial reporting has become important in recent years. Little transparency and low quality of financial information provide conditions that have made decision-making difficult for investors and confront them with ambiguous conditions. Information risk increases in this situation. From view of financial information users, when transparency and quality of presented information is high, information risk of that firm is low. Shareholders and trusters want more and transparent information about firm's performance. Complete disclosure and financial reporting can create secure conditions that increase investors' confidence. Transparency has positive effect on firms' performance and can protect from shareholders' benefits (Kurdistani and Alavi 2012; p: 43). The subject of information disclosure with financial reporting transparency completely and sufficiently in firms' annual reports are effective in decisions of many people in society especially investors in capital market (Chiang 2005). In last decade, national and international financial markets are faced with many financial crises. One reason for these crises is the lack of enough and transparent financial information (Sridharan, Dicsis and Kaynez 2002). In today's turbulent environment, many investors pay attention to significance of information clarifying in their strategies. The lack of information or non confidence about them has become a radical problem in financial markets (Admetti and Fleidrer 2000). Transparent and comparable financial information is the basic of aware economical decisions and responsiveness. Capital owners, trusters and other users for decision- making about purchase, sale, maintaining shares, giving loan, evaluating managers' performance and other economical decisions need understandable and relative financial information (Reza Gholamalipour 2005).

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