Evolving roles of accountants as resources for greater accountability in financial reporting, legislative and judicial processes

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Evolving Roles of Accountants as Resources for Greater Accountability in Financial Reporting, Legislative and Judicial Processes

(Chapter contribution: Value Relevance of Accounting Information in Capital Markets)

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A Introduction to the Volume

The important role which auditors serve in facilitating good corporate governance practices, the monitoring of directors and management of an enterprise, ensuring accountability through the provision of a „true and fair view" on the financial statements of an enterprise, all constitute means whereby the auditor provides important vital, reliable and relevant information and indicators to current and potential stakeholders of an enterprise.

The collapse of Enron demonstrated that not only the traditionally recognized stakeholders namely investors, creditors and employees are affected by such collapses, but that they affect the general public, namely, the average man and woman in the street. In other words, the collapse of Enron has highlighted the move, over the years, from the traditional principal agency model where shareholders constitute the principal stakeholders, to the broader stakeholder model – which focuses on a greater extent, on corporate social responsibility.

Value relevance approach "measures both relevance and reliability because accounting information is reflected in the price." (Khanagha, 2011; Barth, Beaver & Landsman, 2001). Further, "value relevance approach is an instrument used to estimate quality of accounting information – this being of vital importance to the economy."

„An efficient market is one in which security prices adjust rapidly to the infusion of new information, and current stock prices fully reflect all available information including the risks involved. „ (Reilly, 1989).

Financial scandals such as that of Enron have resulted in more stringent audit liability measures in the form of higher corporate governance and auditing standards (Doralt & others, 2008). Corporate governance is defined by the Cadbury Committee as "the system by which companies are directed and controlled". The Sarbanes – Oxley Act of 2002, a post Enron development, has not only increased audit committees' responsibilities and authority; financial services firms with a US listing are not allowed to have their auditors undertaking consultancy work. Whilst audit liability should not be imposed to such extent that it results in defensive auditing (defensive

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auditing being referred to as a practice whereby auditors, rather than exercising their professional judgment, resort to excessive application of rules or audit standards as a means of justifying the results of the audit report), external auditors should still be held accountable for consequences resulting from negligence on their part.

Improved transparency and comparability of accounting and financial information, as well as other benefits of high quality standards which should be derived from the adoption of IFRS: benefits such as improved attributes of information (such as relevance, reliability, understandability), will certainly ensure that users of financial information benefit from better decision making as well as restoring the confidence of investors in the aftermath of economic, capital market and financial crises, which have damaged the credibility of audits, and financial reporting.

B Objectives and Scope

Objectives of this volume include the following:

Objectives of the Study

1) To investigate the extent to which accounting information can be relied upon based on given market values and whether a relationship or pattern can be established in certain jurisdictions based on given operating variables which function in such economies. 2) To demonstrate and highlight the validity of the Efficient Markets Hypothesis (as well as the Efficient Capital Markets Hypothesis) 3) To demonstrate how accounting information can serve as a useful and vital indicator which will enable investors to interpret financial information in such a way which mitigates information asymmetries between management and investors 4) To highlight those areas and factors which influence the quality of accounting information - and which must be addressed by markets if the audit is to achieve its intended aims and functions 5) To highlight whether accounting reforms undertaken in investigated jurisdictions actually achieved their desired goals of improving the quality of accounting information and if such reforms were not successful, to propose measures which could address the current issues being faced by such jurisdictions.

In accordance with the subject matter of the volume, namely the investigation of the value relevance of accounting information in jurisdictions which are more inclined towards capital based market economies - as well as concentrated ownership structures, objectives of the volume will align with the following definition of value relevance, namely, Khanagha (2011):

- the evaluation of the relationship between accounting information and capital market values (market values).

C Research Questions

In line with the research objectives which will be highlighted shortly, research questions to be addressed follow thus:

1) What is the extent to which accounting information can be relied upon based on given market values and can a relationship or pattern be established in certain jurisdictions based on certain operating variables which function in such economies?

2) How valid and applicable is the Efficient Markets Hypothesis (as well as the Efficient Capital Markets Hypothesis) in these jurisdictions?

3) How can accounting information be harnessed in such a way as to serve as a useful and vital indicator which will enable investors to interpret financial information in such a way which mitigates information asymmetries between management and investors?

4) What factors influence the quality of accounting information - and how can these be addressed by markets if the audit is to achieve its intended aims and functions?

5) Have accounting and legislative reforms undertaken in investigated jurisdictions actually achieved their desired goals of improving the quality of accounting information? If not, what measures could be proposed or recommended to address the current issues being faced by such jurisdictions?

D Gaps in the Literature on Topic of Value Relevance of Accounting Information - Conceptual, Theoretical and Empirical Frameworks

Even though various studies have been carried out on value relevance accounting [these including those undertaken by Graham, King and Bailes (1998), Filip & Raffournier (2010), Qystein, Kjell & Saettem (2007) and Khanagha (2011], more recent research is needed in this area - particularly as a means of corroborating the value of audits as signaling mechanisms and the need for such corporate governance mechanisms in predominantly based capital market economies - as well as family and concentrated ownership systems and structures. Information derived from such investigations will also serve as a basis and rationale for fostering initiatives which are not only aimed at improving audit quality in major economies, but also an impetus for investors to engage in corporate governance enhancing negotiations with directors and management of a firm - since greater credibility and environment founded on trust will be facilitated where it is proven that accounting information does have value relevance and can be relied upon.

Beaver (2002) indicated that the theoretical groundwork of value relevance studies adopting a measurement approach is a combination of valuation theory plus contextual theory and financial reporting arguments (accounting theory) that allows the researcher to predict how accounting variables and other information relating to market value will behave. Holthausen and Watts (2001) suggest that value relevance studies use two different theories of accounting and standard setting to draw inferences:

- Direct valuation theory and Inputs-to-equity valuation theory.

As already highlighted, value relevance approach "measures both relevance and reliability because accounting information is reflected in the price." (Khanagha, 2011 ; Barth, Beaver & Landsman, 2001). Further, "value relevance approach is an instrument used to estimate quality of accounting information – this being of vital importance to the economy." This view is in line with the Efficiency Market Hypothesis (EMH).

In line with the observations highlighted under this section, this volume therefore aims to attract qualitative, as well as empirical-quantitative based research on the topic.

E Conclusion

Audit and Accounting has continually proven to be a significant field and contributor in the recent Financial Crisis, and corporate collapses. Audit quality has consequences for corporations as well as investors, since audits serve as vital signaling mechanisms which convey sensitive information to the financial markets and investors alike.

Van Akkeren, Buckby & MacKenzie (2013) argue that there remains some confusion on what constitutes the role of a forensic professional.

It is very well the case that clarity of the definition of what constitutes the role of a forensic professional is crucial to determining how effectively such a role can be harnessed. As well as exploring the various roles undertaken by forensic accountants based in the US and other selected common law jurisdictions, this volume also aims to contribute to the extant literature on how the role of a forensic professional, having evolved over recent years, can be effectively utilized and applied, from common, civil law, as well as comparative based perspectives.

In so doing, the volume also aims to highlight how a greater degree of accountability and transparency can be introduced into the financial reporting process.

With primary reference to stock markets, the topic is not only significant from the perspective of recent developments in the global economy and stock markets across the globe – as evidenced by recent stock market crashes around the globe, but also from the potential of forensic accounting to address vital issues through its investigative techniques.

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