

# QUALITATIVE CHARACTERISTICS OF ACCOUNTING INFORMATION AND THE CONCEPT OF TRUE AND FAIR VIEW – FAIR PRESENTATION

## CARACTERISTICILE CALITATIVE ALE INFORMAȚIEI CONTABILE ȘI CONCEPTUL DE IMAGINE FIDELĂ – PREZENTARE FIDELĂ

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**Abstract:** *The financial information is useful in the process of decision for the company's partners according as these satisfy certain qualities. The qualitative characteristics represent the attributes which establish the utility of the information offered by the financial statements. The General Cadre of International Accounting Standards Board (IASB) has identified the next characteristics: understandability, relevance, reliability, comparability of the financial information. The usefulness of the economics and financials information is a combination of the foregoing qualitative characteristics and it generate more satisfaction for its users. The quality of the information offered of the financial statements lead to true and fair view. The General Cadre of IASB doesn't use the true and fair view notion, but it indicate the financial statements must represents a real and correct view or present trustily the financial position, the performance and the modifications of the financial position. The concept of the true and fair view is regulated through 4<sup>th</sup> Directive of the European Union and one of fair presentation through IAS 1. Indifferently of mode in which it is named this concept - true and fair view or fair presentation – it wants to obtain the true in accounting.*

**Rezumat:** *Informațiile financiare sunt utile în procesul decizional al partenerilor întreprinderii în măsura în care acestea satisfac anumite calități. Caracteristicile calitative reprezintă atributele care determină utilitatea informațiilor oferite de situațiile financiare. Cadrul general al Consiliului pentru Standarde Internaționale de Contabilitate (IASB) enumeră următoarele caracteristici: inteligibilitatea, relevanța, credibilitatea și comparabilitatea informațiilor financiare. Utilitatea informațiilor economico-financiare reprezintă o mixtură a caracteristicilor calitative menționate și generează un plus de satisfacție pentru cei ce le folosesc. De calitatea informațiilor furnizate de situațiile financiare depinde obținerea imaginii fidele asupra activității oricărei întreprinderi. Cadrul general al IASB nu abordează în mod direct noțiunea de imagine fidelă, menționând faptul că situațiile financiare trebuie să redea o imagine reală și corectă sau să prezinte fidel situația financiară, performanța și modificările poziției financiare. Conceptul de imagine fidelă este reglementat prin Directiva a IV-a a Uniunii Europene, iar cel de prezentare fidelă prin IAS 1. Indiferent de modul în care este denumit acest concept – imagine fidelă sau prezentare fidelă – el vizează obținerea adevărului în contabilitate.*

The last decades of economy development in the world are characterized by an acceleration of the internationalization of capital markets and commerce. The

ever higher degree of globalization of capital markets imposes the worldwide use of a unique language for financial reporting, so that the world's economic system would benefit from credible and transparent accounting information.

The objective of financial statements is to provide information regarding financial position, performances, and the modifications of the financial position. This information is useful to a large palette of users, for motivating their economic decisions.

The requirements for qualitative financial information appeared in the United States of America after the economic, financial, and stock exchange crisis in 1929, when investors had insufficient information (Ștefănescu, 2005). The first step in this direction has been the creation of financial norms, imposed on companies that issued negotiable securities, and later the FASB – Financial Accounting Standards Board has issued the accounting norm SFAC 2 “Qualitative characteristics of accounting information”.

## **MATERIAL AND METHOD**

The qualitative characteristics are the attributes that determine the usefulness of the information provided by financial statements. The collection, processing, and communication of the information in the balance sheet are directed by a set of norms, regulations, and procedures.

At the international level, there coexist two dominant accounting streams or systems that have directly influenced the creation and presentation of financial statements. These are:

- The continental accounting system;
- The Anglo-Saxon accounting system.

In what concerns the approaches of the two accounting cultures, there are multiple and important differences, which has lead to the initiation of processes of balancing and filling in the gaps. One of the most significant differences that have appeared between the two streams regards the concept of faithful image. While in the Anglo-Saxon accounting system the faithful image is the supreme principle, the continental approach considers it the fundamental objective of financial accounting.

## **RESULTS AND DISCUSSIONS**

The general frame of the International Accounting Standards Board – IASB mentions the following characteristics: intelligibility, relevance, credibility, and comparability of financial information.

***Intelligibility*** means that financial information has to be easily understood by the users of financial statements. Not all the information is accessible for any user category. For this requirement to be met, users are supposed to have sufficient knowledge regarding the business process and the economic activities, to master accounting notions, and to have the desire to study the information presented. This does not mean that the information with a higher degree of complexity do not have to be expressed in financial situations.

***Relevance*** refers to the ability of the financial information to influence the economic decisions of the users, helping them evaluate past, present, and future

events, confirming or correcting previous evaluations. This allows for an estimation of the company's ability to take advantage of the opportunities and to react immediately to unfavorable situations, as well as for a prediction of the future financial position and performance of the company. Therefore, the relevance of the information has two roles: to predict and to confirm.

*The prediction role* supposes that the present level and structure of the assets have a value for the users when the latter try to predict the company's ability to take advantage of opportunities and to react to unfavorable situations.

*The confirmation role* supposes that this information is meant to confirm previous predictions (for example: the way in which the company can be structured, or the result of the planned activities). The information concerning the financial position or previous performances are frequently used as a basis for predicting the future financial position and performances, as well as other problems of direct interest to the users, such as: payment for dividends and salaries, variations in the price of certificates, as well as the ability of the company to meet its due obligations. From this point of view, "accounting standards have the role to ensure the relevance of accounting information provided by financial statements for the decisions of investors and of other users. For example, creditors use financial information to evaluate the company's ability to meet future obligations. Information about the past is often useful to creditors for predicting future cash debts, as well as cash incomes. The reported information regarding current and long-term debts, as well as specific sources, can be used to calculate the company's financial rates and the weight of the assets of the society financed from debts." (Dycman, 1995).

**Credibility** means that the information presented does not include significant errors, and that it is not subjective, so that the users can be confident that it correctly represents what it is meant to represent or what is reasonable expected to represent.

In order to be credible, any information has to take into account: faithful representation, the prevalence of substance over form, neutrality, prudence, and wholeness.

*Faithful representation* is the characteristic through which some credible information has to faithfully represent the transactions and other events. For example, the balance sheet has to display in a credible manner the transactions and events of the company expressed in assets, debts, and owned capital at the date of the report, if they meet the criteria for recognition.

*The prevalence of the substance over form* is also expressed in French as "la prééminence du fond sur la forme" and it refers to a prevalence of the economic details over the juridical ones (Horomnea, 2004).

This characteristic aims to point out the fact that certain transactions or events are not always according to what results from their juridical expression. For instance, if a company gives away an asset to another party, so that the documents express the transmission of the copyright to that respective party, there can exist contracts that give the company the right to enjoy future economic

benefits from the respective asset. In such circumstances, reporting a sale would not represent in a credible manner the completed transaction. The most relevant case is that of the leasing contract, especially that of operational leasing.

*Neutrality* implicitly states that the information is objective, free from influences. Financial statements are not neutral if they influence the making of a decision or the formulation of a pre-determined professional reasoning.

*Prudence* means including certain precautions in applying professional theories necessary for making the estimations required in uncertain conditions, so that the assets and the incomes are not over-valued, and the liabilities and debts are not under-valued. Financial statements have to overcome uncertainties that affect events and transactions, such as: cashing uncertain debts, the probable usage duration for devices and equipments, the number of complaints regarding the products in guarantee. All these uncertainties are recognized through the presentation of their nature and value, practicing prudence in drawing financial statements.

However, using prudence does not presuppose creating excessive provisions or reserves, deliberate under-evaluations of the assets and incomes, or an over-evaluation of debts and expenses.

*Integrity* supposes that, in order to be credible, information in financial statements has to be complete, within the reasonable limits of the threshold of significance and of the cost of its raising. Omissions make information become fake or misleading, so that it is no longer credible, and it becomes defective from the point of view of its relevance.

The general frame of IASB presents the characteristics of relevance and credibility and the interrelations between them, showing that they are useful taken individually, but their usefulness is more appropriate if a series of restrictions are observed, such as: opportunity, the cost-benefit ratio, the balance between qualitative characteristics, faithful image / presentation.

*Opportunity* means that if there is an exaggerated delay in information reporting, it loses its relevance. There are situations when the management has to choose between two variants: the relative value of a report and the provision of credible information.

*The cost – benefit ratio* represents more of a constraint than a characteristic, as the benefits of the information should be higher than the cost of their production.

*The balance between qualitative characteristics* is necessary in order to meet the objectives of financial situations, and it also represents an issue related to professional thinking problem.

*The faithful image/ presentation* suppose that the application of the main qualitative characteristics and of the appropriate accounting standards normally results in drawing financial statements that reflect a faithful image of the company's situation.

*Comparability* proves useful when it is required to identify the tendencies in the financial position and performances of the company. Any information is

more valuable if it can be compared in time or space, respectively, if it can be compared to other reference values. The measurement and presentation of the financial effort of the same events and transactions have to be done in a coherent and unitary manner, both within a company, in time, and in other companies at the same moment.

The importance of comparability resides in that the users need to be informed about the accounting policies used in making the financial statements, the changes in these policies, the effects of these changes, so as to be able to identify the differences between the accounting policies used in a company at various moments, as well as between those used in various companies.

The qualitative characteristics of the accounting information provided in annual financial situations lead to a faithful image on the activity of any company.

The general frame of IASB does not approach directly the notion of faithful image, mentioning that financial situations have to render a real and correct image, or to faithfully present the financial situation, the performance, and the changes in the financial position. Such an objective is met through the four compulsory characteristics of the information provided in financial statements.

In an accounting system based on normative regulations, as is the national accounting system, a faithful image is presented by observing the requirements for regularity and honesty, where regularity refers to observing the applicable accounting rules and procedures, and honesty, to their faithful and professional application. The two components of a faithful image should lead to obtaining financial situations that provide real and useful situations for their users.

Article 2 of the 4<sup>th</sup> Directive of the European Union states the following rules regarding the faithful image:

- Annual accounts include the balance sheet, the profit and loss account, and the annex. All these represent a unitary whole;
- Annual accounts have to be clearly established, in conformity with the present directive;
- Annual accounts have to render a faithful image of the patrimony, of the financial situation, and of the result;
- If the application of the present directive is not sufficient to render a faithful image, supplementary information has to be provided;
- If in exceptional cases the application of a disposition in the present directive does not lead to a faithful image of financial situations, derogation from this disposition is required, which should be mentioned in the annex and appropriately supported.

The faithful presentation is regulated by IAS 1, which states that:

- Financial statements have to be according to the significant accounting dispositions of the IAS;
- The faithful presentation does not exclude the possibility of transgressions of certain requirements of the IAS;

- In order to ensure a faithful and complete image regarding the financial position, the performance, and the cash flows, the application of the IAS does not exclude the possibility of supplementary information;
- Inappropriate accounting statements cannot be corrected neither by presenting the accounting policies used, nor through grades or explanatory materials;
- It is required to present the cases when certain dispositions of an IAS are applied before the date of applicability of the respective IAS.

## CONCLUSIONS

The usefulness of economic and financial information is a mixture of the qualitative characteristics mentioned and generates extra satisfaction, which in specialized literature is called “non-quantifiable benefits” (3). In the hierarchy of these characteristics, the usefulness shifts between the higher or the lower weight given to relevance or to credibility.

As a result of the qualitative characteristics of the information provided in the company’s financial statements, the concept of faithful image – faithful presentation refers to obtaining the truth related to accounting, which is a relative notion from a philosophical point of view, as the subject field of accounting is no exception.

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