ZARIFIAN, PH. (1999). *Objectif : compétence : pour une nouvelle logique.* Editions Liaisons. Paris.

António Martins

PERCEPTIONS OF THE QUALITY OF FINANCIAL INFORMATION IN PORTUGAL

Резюме

Эта статья посвящена качеству финансовой информации и ее влиянию на процесс корпоративного управления. Рассматриваются две главные темы. Во-первых, обсуждаются причины недавно произошедших случаев корпоративного управления, которое несоответствует общепринятым правилам. Во-вторых, проанализировано восприятия качества финансовой информации в ходе вышеупомянутых скандалов.

Статья основывается на изучении восприятия человеком надежности финансовой информации и ее влияния на качество процесса управления. В роли опрашиваемых выступали португальские студенты старших курсов и финансисты-профессионалы.

Главные выводы статьи – респонденты имеют существенно отличающееся восприятие качества информации, публикуемой различными компаниями. Проверка представляется как релевантный механизм для улучшения качества финансовой отчетности. Примечания к финансовым декларациям расцениваются как самый достоверный источник финансовой информации; балансу предприятия (как финансовой документации) доверяют больше, чем декларации о полученных доходах. Манипулирование рассматривается как вторжение в область финансовой информации; предложенные реформы предусматривают усовершенствование финансовой отчетности, принятие международных стандартов отчетности, предлагая пенальти менеджерам, которые ответственны за публикацию «манипулирующей» информации. Из всех стран Германия, Франция, Австралия и Япония имеют финансовые информационные системы, вызывающие наибольшее доверие.

1. Introduction

Corporate governance is widely perceived to be in a troubled state in developed market economies. Recent scandals in major financial markets – like Enron, Worldcom, Tyco, Parmalat and others – diminished the confidence in good company governance.

Some of the core foundations of corporate governance were held hostage to special interests, and a set of entities like stock analysts, banks, brokers and auditors colluded to deprive shareholders of their fair share of firms´ results. (Levitt, 2002; Monks and Minow, 2001).

Financial fraud is not a new or unexpected event in economies where so much depends on the financial performance of corporations. Schilit (1993) documents several cases of manipulation of financial information during last century. Boatright (1999) presents evidence of conflicts of interest in financial services and financial markets. Chancelor (1999), analysing the history of financial speculation, documents unethical behaviour of market participants since the 17th century. What seems to be new at the beginning of this century is the scale and the global nature of the phenomenon.

The quality of corporate governance, strongly linked to the future of many people in major developed economies, is thus a topic that merits further discussion. Workers´ jobs and remuneration are obviously related to the decisions taken by people charged with governance tasks in companies; pensions of elderly people are affected by the stock market performance of firms; the degree of perceived fairness and social acceptance of capitalism is also dependent of the integrity of its captains of industry; and the efficiency of resource allocation through investment and financing decisions is also closely associated with good corporate governance.

This paper focuses on the quality of financial information and its impact on corporate governance, and addresses two major questions. Firstly, it will discuss the reasons for the recent occurrence of several cases of inappropriate corporate governance. Its causes will be dissected and the role of boards of directors and auditors will be of special interest, as it seems that those two entities were at the root of many problems, or, at least, did not exercise their control duties regarding to executives. Then, the new regulatory framework that is emerging to check these problems will be discussed.

A second purpose of the paper is to analyse perceptions about the quality of financial information in the wake of the aforementioned scandals. It will present a survey of people's perceptions about the reliability of financial information and its influence on the overall quality of the governance process. The survey will be based on two samples: the first consists of undergraduate students that have been exposed to the conceptual aspects of financial information and governance; the other will consist of professionals that must deal with daily life situations where most potential sources of problems arise. Questions like the perception of the quality of financial information in different types of companies, the impact of auditing in information quality, areas where rules are more easily bent, and areas where regulatory reform is needed will be of particular interest.

The main conclusions of the paper are that surveyed persons have significant different perceptions about the quality of information published by different types of firms and that auditing is seen as a relevant mechanism for improving the quality of financial reporting. Notes to financial statements are regarded as the most reliable source of financial information and balance sheet is more trusted than income statement. Manipulation is seen as a pervasive situation so far as financial information is concerned. When questioned about reforms to improve financial reporting in Portugal respondents advocate stronger penalties to managers who authorise the publishing of manipulated information and the adoption of International accounting standards. Among a large group of countries, Germany, France, Australia and Japan have the most trusted financial information systems.

As a contribution, I expect that a better knowledge of perceptions about the quality of financial information and its impact on corporate governance is helpful to academics, executives, regulators and investors.

The paper is organised as follows: section 2 presents a brief survey of financial scandals and its roots, section 3 focuses on the new regulatory framework arising in the wake of the Sarbanes-Oxley Act, section 4 presents survey results, section 5 concludes.

2. Uses and abuses of financial information: a short note

Financial information45 plays a vital role in the process of corporate governance.

Channels of influence of financial information into the governance mechanisms include its effects on the operation of control mechanisms between principals and agents46, and the reduction of asymmetries of information between interested parties in the financial performance of firms. These function are essential in a market economy, mainly in the area of identifying investment opportunities to allocate scarce resources and to choose how to finance projects.

The operation of control mechanisms based on accounting information is well documented in research literature47. For example, its role on takeovers is documented in Palepu (1986), its impact on shareholder litigation is presented in Skinner (1994) and its influence in the designing of debt contracts is analysed in Sweeney (1994).

Also, research by LaPorta *et al* (1998) shows that the governance role of financial accounting information is very important to the economic performance of countries. Rules of investor protection and the limiting of expropriation by insiders are thought to be quite influential on the efficiency levels of financial markets and to the proper allocation of resources.

If financial information has such a vital role, it is not surprising that it can be (mis)used to the benefit of corporate insiders at the expense of outside investors. Chancellor (1999) presents several cases of misrepresentation of financial information aiming at expropriation of outsiders by company insiders. The author begins by presenting the excesses of the tulipmania in Amsterdam48, in the 17th century, and then turns to the emergence of London stock market and describes its first bubbles. The South Sea bubble, the speculation related to the apparently promising markets of newly independent South American countries49 , and the railway mania, all share the traits of schemes devised by insiders who controlled information and then sold worthless securities to outsiders.

In more recent times, the scandals uncovered at the end of the so-called “roaring eighties”, where Michael Milken, Ivan Boesky and other finance professionals were major players, were a severe blow to the faith in the good functioning of capital markets. It seemed that ethics was increasingly absent from the corporate executive suites, from the market trading floor or from bank boardrooms.

The 90s began with a sense of uneasiness about the level of fairness of capital markets and a feeling that corporate governance rules were serving insiders at the expense of outsiders. Printed stories of the excesses of the 80´s – like the one told by Burrough and Helyar (1990) about the leveraged buy out of RJR Nabisco – seemed to confirm the scepticism about the role of ethics in financial markets and corporate governance practices.

Then, in 1995, the IPO of Netscape launched a new era of euforia50, that ended in early 2000 when the Nasdaq index crashed. The mantra of his new era was that “this time is different”, and the difference got even a glamorous name: the “new economy”.

The sensation that the “new economy” companies were so prone to the misuse of financial information was a growing feeling towards the end of the 90´s; but it become all to clear at the bursting of the bubble when major scandals like Enron, Worldcom, and others emerged.

Few authors were so well placed to document the growing trend of abuses of financial information and corporate governance than Arthur Levitt. I will thus rely mainly on Levitt (2002) to characterise that period. Arthur Levitt was the chairman of the Securities Exchange Commission from 1993 to 2001, and had to deal with a lot of issues related to financial information and its use in the corporate governance process. Issues like the expensing of options51, the regulation of full disclosure52, the separation between auditing and consulting activities of the then “big five” multinational audit firms53 were under intense scrutiny of politicians, lobbyists, executives.

[45] “Financial information” is here defined in the sense of Bushman and Smith (2002) as the product of corporate accounting and external reporting systems that measure and publicly disclose audited, quantitative data concerning the financial position and performance of a publicly held firm.

[46] A classical example of this function is the performance related pay of executives, where performance is measured by some accounting numbers.

[47] Bushman and Smith (2002) was especially helpful in documenting research trends in financial information related to governance aspects.

[48] In this context, Chancellor refers to the statement of a Spanish author – Vega – related to the way the Amsterdam market operated. He says that “ the expectation of an event creates a much deeper impression upon the exchange than the event itself”.

[49] Chancellor refers to a prospectus of a company that stated that its purpose was “ to carry an undertaking of great advantage but no one to know what it is”.

[50] Obviously that the precise moment when a new speculative era begins is quite difficult to define and is open to debate. The internet and related technologies were available before; but the contagious effect of the so–called “net stocks” in the development of world stock markets in the second half of the 1990s is generally associated with the decision of the Netscape board to launch an initial public offering for a company with no earnings history and that was overbooked by eager investors. This is now seen as the moment when the “everything is possible” sentiment of “dot com” companies began. See Cassidy (2002) for a detailed account of this phenomenon.

[51] The proper accounting treatment of stock options granted to executives and workers generated a hot debate between academics, Silicon Valley entrepreneurs and SEC officials. Many accounting and finance academics argue that options should be expensed, but the new economy entrepreneurs and their lobbyists in Washington pressed for a treatment that did not affect the net income reported by firms.

His view of the main forces shaping the financial environment faced by investors and the potential for misrepresentation of financial information is summarized in the following statement:

" When I arrived at the SEC, in July 1993, we were in the third year of a bull market ... On the surface, everything seemed fine. But there was much about Wall Street and corporate America that made me uneasy. …many CEOs were paying more attention to managing their share price than to managing their business. Companies technically were following accounting rules, while in reality revealing as little as possible about their actual performance. The supposedly independent accounting firms were working hand in glove with corporate clients to try to water down accounting standards" Levitt (2002: 7/8).

When the SEC chairman tried to change rules and increase auditor´s independence, his proposals were undermined by the Congress, which oversees SEC. He published convincing evidence that many Congressmen were acting in the interests of the then Big Five, which lobbied hard against the proposals that would deprive them of important consulting revenues54.

But investors were not only at the mercy of executives and auditing failures. Other intermediaries between firms and shareholders – like analysts – become prey to investment banking pressures to propel share prices. Research was increasingly seen as mere tool for deal making between banks and firms, and sell recommendations become more rare55. The leaking of estimations of earnings to selected analysts become widespread, and the companies managed expectations just enough to "beat the consensus estimates"56.

The role of analysts in the market euphoria that happened in the US at the end of last decade was even more marked in the IPOs of "dot com" firms. The one that epitomizes the new approach was Mary Meeker, at that time at Morgan Stanley investment banking, and dubbed " Queen of the Net". During the "dot com" boom valuations rose to limits that could not be explained by standard models of discounting expected cash flows at the appropriate cost of capital. Analysts had to imagine new ways of rationalising those prices. And duly they did.

The key insight of analysts was that valuation should rely on earnings that those companies could produce in the distant future, and, in order to achieve that potential, burning money and producing losses in the present were seen as preconditions to build a customer base. Thus, the apparent absurdity of firms that produced ever increasing losses and had ever increasing share prices was, at least, not so disturbing.

Investment bankers quickly saw that analysts could be used as marketing tools. The process worked like this: an analyst would be assigned to value a firm and came up with a report that would support a convenient share price that, in the Initial Public Offering (IPO), generated a hefty commission for the bank that employed the analyst. Then, the analyst continued to cover the stock and would maintain a buy recommendation, and the next round of financing would be arranged by the bank. The "dot com" executives had a strong interest in producing numbers that supported the share price, in order to cash in on large amounts of stock options.

The new mood about valuation those days is well illustrated by Meeker´s statement, in 1997, saying that stocks "entered a new valuation zone"57.

One particular abuse of financial information in this period was linked to the fact that executives were eager to use earnings guidance to support share prices, because so may firms were using options as a way of compensation.

The relevance of managerial forms of compensation to corporate governance has its roots in the well known agency theory, which can be traced back to Bearle and Means (1932). The separation from ownership and control creates an organizational environment where owners (principals) must have some form of aligning the actions of managers (agents) with their interests. Based on the work of Jensen and Meckling (1976) an extensive body of research documented several types of agency costs and proposed new solutions to mitigate the agency costs created by modern forms of management of public firms.

According to Bushman and Smith (2002) the main conclusions of this research literature can be summarised as follows:

i) Financial accounting measures are widely used in executive compensation contracts58;

---

[52] Regulation of full disclosure was approved by a majority vote in October 200 by the SEC. It requires that companies should release important information to all investors and not just to a selected few. Such "selective disclosure" put small investors at a disadvantage to analysts, brokers, and other more powerful entities.

[53] As the new economy era progressed, it was becoming clear that soft auditing was spreading and that the consulting fees earned by the big five were hampering their duties of proper auditing. Management actions and financial information were not checked by auditors; they were acting more as advisors on financial schemes aimed at supporting share prices.

[54] See Levitt (2002: 287-307). It is therefore no surprise when he says: " Two things, I have learned, defy the political process: closing military bases and setting accounting standards …The debate on stock options is a perfect example".

[55] For a detailed account of this process, see Boatright (1999), Cassidy (2002) and Levitt (2002)

[56] The release of earnings is usually a very important event for firms and investors. As share prices should reflect an estimation of the earnings growth rate, missing that target can trigger significant adjustments. CEOs and CFOs were thus under pressure not to miss the targets. Another reason was that their options value would be severely punished with a decline in the stock price.

[57] The complete statement – from Cassidy (2002) – is :" We have one general response to the word "valuation" these days: bull market. We have been in the technology sell-side trenches for about a decade and simply –we believe that we have entered a new valuation zone. In addition to valuations being a function of a happy market, this zone is also a function of the Internet".

[58] The authors cite empirical evidence based on surveys of publicly traded US companies about their compensation plans presented by Itner et al (1997) do confirm the importance of accounting numbers in executive compensation plans.

ii) In the last three decades of the 20th century accounting measures have lost importance in influencing compensation of executives, as these plans shifted towards other measures. The major trend have been the extensive reliance on stock and stock options as compensation mechanisms59;

iii) Changes mentioned in ii) were more pronounced in firms with higher growth opportunities.

The reliance on accounting numbers to determine executive compensation creates potential opportunities for the misrepresentation of financial information by executives. Sales, net income or rates of return, to mention some of the common measures, are numbers whose computation depends on the practical application of accounting principles and rules.

Even when the weight of compensation policies moves towards stock and options, the problem of misuse of financial information does not vanish. The role that reported earnings play on influencing stock prices makes earnings management a prime target for some executives.

Public companies have control mechanisms that can act as a counterweight to executive temptations: boards and auditors are two of the most important.

However, the effectiveness of boards was seriously questioned by the emergence of a wave of scandals in the aftermath of the stock market bubble of the late 90s. The degree of independence of many boards seemed to have been greatly diminished by the grip that top management had on board functioning. Board members with consulting contracts with companies they were overseeing, the use of corporate perks, the use of corporate donations to institutions where board members had interests and other ways of limiting independence produced an environment skewed towards favouring executives´ power at the expense of investors.

Levitt (2002) points to several aspects that outsiders must carefully scrutinise in order to assess board effectiveness: the degree of independence, the commitments of board members and its impact on their capacity of really perform their controlling functions with time and technical expertise, board size and board compensation and perks.

But some of the problems that plagued board effectiveness in controlling executives were also common in the relation between executives and auditors.

In capital markets, investors grasp of firms performance by relying on published financial information is critically affected by the quality of auditing. The growing importance of consulting contracts and the fatter margins earned on consulting relatively to auditing, made some auditing firms too prone to engage in consulting contracts with management of public firms.

Publicly, the argument for this state of affairs was that the deeper knowledge of public firms structure allowed by auditing was an useful element in performing consulting tasks like information systems design, and tax planning or strategic advice. But, in reality, the independence of the audit function was severely compromised by the fear of losing lucrative consulting fees.

Earnings management activities had, in many cases, no checking entities. Analysts were under investment banks overriding aim of not to endanger financing deals, board independence was weakened by tying members with generous perks, and auditors were under the stick of losing consulting contracts.

In the aftermath of the scandals that emerged in the US and Europe in 2001 and 2002 – like Enron, Worldcom, Tyco, Health South or Ahold – there was a public outcry. The US Congress rushed to enact new legislation to limit the abuses of corporate executives´ power.

The new regulatory environment that resulted form these activities is the topic for next section.

3. A new regulatory framework

In the light of the scandals emerging in US, a strong reaction by Congress produced – in a very short time – the Sarbanes-Oxley Act, enacted in July 2002. It tried to impose strict rules on financial disclosure and the corporate governance process.

In its section 201, the Act prohibits auditors of rendering non audit services, and, also, in sections 203 and 206, deals, respectively, with auditor rotation and conflicts of interest in hiring auditing firms if the CEO, CFO or Controller worked for the audit company for one year before the audit.

Section 302 establishes corporate responsibility for financial reports, and sections 401 and 402 enhance disclosure rules by firms, like off balance transactions and personal links between firms and executives.

The auditing committee is also strenghtened (section 407), and analysts conflicts of interest are covered in section 501, by requiring that SEC produces new independence rules to be applied to the profession. But it is on Title VIII of the Act – “ Corporate and Criminal Fraud Accountability “ – that most significant changes were made. Penalties imposed on fraudulent behaviour of executives, auditors, accountants and others are quite severe. For example, in section 802, the penalty for destruction, alteration or falsification of documents can go to 20 years in jail. In section 906, the penalty for a CEO or a CFO for signing a fraudulent financial report can go up to 20 years in jail.

In Portugal, although nothing similar has been under way, the CMVM (the stock market watchdog) published new rules on “the corporate governance of public companies” in December 2001, updated in July 2003.

The general sense of these rules is to offer better protection to investors, to induce the creation of better internal control systems, to limit the use of “poison pills”, to strenghten the independence of auditing and compensation committees, to publish information on executive pay, to disclose more information to shareholders about

[59] The authors state that “ ...not only have earnings apparently become less important in determining cash compensation, the contribution of cash compensation to the overall intensity of top executive incentives appear to have diminished drastically in recent years. The shrinkage is so dramatic that a number of recent studies on top executive pay- performance sensitivity simply ignore the contribution of cash compensation as a second order effect…”

stock option plans and to encourage institutional investors to have a more involved relationship with the companies where they invest.

It can thus be argued that the wave of scandals created a favourable disposition for reform. Its effectiveness remains to be seen and, presumably, only when the next prolonged market upswing will happen can the new rules impact be tested.

Another important question is the impact of those facts – major failures of governance mechanisms and the new regulatory framework – on public perceptions about the reliability of financial information and firms´ governance process. That is the topic for next section.

4. Perceptions on the quality of financial information

This section presents a survey based on two samples. The first one consists of 100 undergraduate students of Economics and Management courses that, by the time of the survey, had been exposed to Financial Accounting and Financial Analysis courses. They were knowledgeable of conceptual topics related to the production and use of financial information and the majority of them had to deal with financial reports, by using them in case studies. The other sample consists of 76 professionals, graduated in Economics, Management or Accounting that attended post-graduate studies. Both surveys were applied during classes.

By using two samples it can inferred if the quality of financial information is differently perceived by students and professionals. It could be expected that students presented a higher degree of belief in the reliability of financial information, because they have little or no exposition to real life situations that can shake confidence on the quality of financial information. On the other hand, as both surveys were administered in 2003, the set of accounting scandals in US and Europe could significantly affect student's faith in the overall quality of financial information.

Table 1 presents some attributes of surveyed students and professionals.

Table 1. Samples characterisation

		Students (N = 100)	**Professionals (N = 76)**
Gender	M (%)	46,0	65,8
	F (%)	54,0	34,2
Age	Mean	22,85	36,61
	St. dev.	2,31	11,84
Investments holdings	Yes %	33,0	63,2
	No %	67,0	36,8

Females represent 54% of students' sample, but they are only 34,2% of professionals'. It could be a sign that although in the recent years females overtook males in Economics and Management undergraduate studies, the situation is still different at the professional level.

As the mean age of professionals is 36,61 years, the number of females in managerial or other related jobs that require previous Economics/Management studies is lower, because at the time of undergraduate studies (on average, almost 20 years ago) the proportion of male students was higher.

A second factor can also explain the lower proportion of female professionals. It could be hypothesised that, in career development, females have more difficulties in attending post graduate courses, either because career advancing opportunities are more open for men or because family related tasks tend to burden females more often than males.

Another attribute of respondents (holding of financial investments like shares, investment funds, bonds or equity in limited liability companies) is presented in table 1. It shows an expected difference between professionals and students. In fact, only 33% of students hold some type of investments, while 63,2% of professionals do. However, the proportion of students holding financial investments is quite important.

Table 2 presents evidence on the perception of the reliability of financial information published by different types of companies. A scale from 1 – no reliable – to 7 – totally reliable – was used.

Table 2. Perceived reliability of financial information published by type of firm

	Students (mean)	**Professionals (mean)**	**Significant differences (Mann-Whitney test)**
Portuguese corporation not listed in the stock exchange	3,62	3,57	
Small portuguese LLC	3,28	2,64	**
Foreign corporation, operating in Portugal, not listed in the stock exchange	3,73	3,96	
Big Portuguese LLC	4,18	4,09	
Portuguese corporation listed in the stock exchange	4,95	4,99	
Individual entrepreneur	2,77	2,25	**

(**) Significant at 0,01 level

It can be observed that only two types of corporations ("big Portuguese Limited Liability Companies (LLC)" and "Portuguese corporation listed in the Stock Exchange") have mean scores higher than 4, which is the mid point of the scale. These are the only type of companies that have scores higher than 4 in students and professionals samples.

However, the Portuguese listed corporations have the highest score (near 5) in both groups, and they stand out as the sole case of a relatively consistent level of reliability in financial information. The fact that affiliates of foreign companies operating in Portugal have scores lower then 4 can be explained by a certain degree of belief that, as they belong to foreign groups, they could be used for convenient tax or financial planning, diminishing the overall quality of their financial information.

From table 2 it is remarkable (and expected) the "small Portuguese LLC" and "individual entrepreneurs" are the type of firms that produce the least reliable information. However, professionals are more sceptical regarding both, and a significant difference in mean scores is observed.

The overall picture that emerges from table 2 is quite worrying. For the 6 types of firms, only Portuguese listed corporations have some degree of credibility with respondents, and very low scores are observed for small LLC and individual entrepreneurs.

Let us note, however, that as the corporate governance process is more important in public companies, the fact that listed firms are positively rated regarding their financial information by both groups is an encouraging sign.

Table 3 presents evidence on the perceived influence of external auditing on the general quality of financial information.

Table 3. Perceived influence of external auditing on the quality of financial information

	Students	Professionals
Big quality improvement	32,0 %	25,0 %
Some quality improvement	58,0 %	65,8 %
No influence	8 %	7,9 %
Some deterioration of quality	2 %	-
Big deterioration of quality	-	-
No opinion	-	1,3 %
	100,0 %	*100,0 %*

It must be said that as, in Portugal, all corporations and big LLC are audited, it can be expected that there is some relation between tables 2 and 3. If perceptions presented in table 2 – where corporations and big LLC had the better scores – were influenced by mandatory external auditing, then results shown in table 3 should confirm respondents' awareness of auditing relevance. On the other hand, recent accounting scandals exposed big failures in auditors' diligence, and that could tarnish the reputation of auditors. But, as no major auditing scandal has yet emerged in Portugal, results from table 3 are quite positive for the auditing profession, with 90% of both groups assigning "big" or "some" quality improvement in financial information by external auditing.

Tables 4 and 5 present the perceived degree of reliability of different financial statements and accounting aggregates (from 1 – no reliable –, to 7 - totally reliable).

Table 4. Perceived reliability of different pieces of financial information

	Students (mean)	Professionals (mean)	Significant differences (Mann-Whitney test)
Income statement	4,49	4,2	
Balance sheet	4,48	4,05	**
Cash flow statement	4,37	4,32	
Notes to the financial statements	4,86	4,42	**

(**) Significant at the 0,01 level

Table 5. Perceived level of truthfulness in financial statements in different aggregates

	Students (mean)	Professionals (mean)	Significant differences (Mann-Whitney test)
Operating revenues	3,68	4,15	**
Operating costs	3,78	4,16	*
Assets	4,66	4,46	
Equity	4,94	4,65	
Liabilities	4,25	4,44	
Accruals	3,59	3,67	
Financial revenue and costs	3,87	4,47	**
Extraordinary gains and losses	3,31	3,92	**

(**) Significant at the 0,01 level
(*)*Significant at the 0,05 level*

It is interesting to note that, in table 4, all financial statements and their related notes score between 4 and 5. It is also worth noting that students have more positive perceptions across the four alternatives. And, regarding "balance sheet" and "notes to financial statements", there are statistically significant differences between students and professionals.

One important conclusion stands out from table 4: notes to financial statements are the most trusted source of financial information for both groups.

As every user of a financial report knows, “notes” are, most of times, the only way to understand the numbers presented in financial statements, and must be carefully interpreted to gain a better perspective of raw numbers. It seems that students and professionals are quite aware of that.

Table 5 shows the perceived level of truthfulness in different accounting aggregates.

It is interesting to note that in the balance sheet – which contains, as it is well known, assets, accruals, equity and liabilities - accruals are the only one item that scored less than 4. Other balance sheet aggregates are marked higher than 4 by students and professionals. The widespread perception that accruals can be used to influence earnings is certainly at the root of this result.

It is in the revenue and cost areas that groups’ perceptions mostly differ. Students have a more pessimistic view of the truthfulness in reporting revenues or costs, be it at the operating, financial or extraordinary level. “Extraordinary gains and losses” are the least trusted areas for both groups, in terms of revenues and cost aggregates. And, in the professionals’ group, only “accruals” have a lower score.

Table 6 presents respondents’ views about the frequency of manipulation of financial information.

Table 6. Overall perception of frequency of manipulation in financial information

	Students	Professionals
Always	6,0 %	6,6 %
A lot of times	87,0 %	82,9 %
Some times	5,0 %	10,5 %
Never	-	-
No opinion	2 %	-
	100 %	*100 %*

Results are quite similar for both groups: 93% of students say that financial information is manipulated “always” or “a lot of times”, while 89,5% of professionals say the same. No one said “never”!

A widespread feeling of manipulation of financial information is a severe blow to the faith in corporate governance mechanisms, and can inhibit potential investors from participating in the development of financial markets.

How can we square the results from table 6 with the more positive results from table 1? In table 1, the better rated companies – according to the reliability of financial information – were big LLCs and listed corporations. As it is well known, Portugal is a country of micro and small enterprises. Only a few dozens of corporations are listed in the stock exchange. This being so, the perception of manipulation is probably related to the large numbers of small firms where there is a wide perception of manipulation. Table 7 shows some possible causes for manipulation and respondents´ views about their relevance, from 1 (not relevant) to 7 (very relevant).

Table 7. Relative importance of possible causes of manipulation in financial information

	Students (mean)	Professionals (mean)
Improvement of external image of firm to banks, customers and investors	5,53	5,48
Tax avoidance	6,23	6,00
To increase performance related pay	4,23	4,40
To hide management difficulties on running firms	4,88	4,68
To please shareholders	4,65	4,81

Tax avoidance stands clearly as the main cause of manipulation of financial information. Given the well known anomalous situation of the corporate income tax (IRC), where about 60% of companies do not pay any profit related tax, the result is quite natural.

The second most important reason is “to improve the external image of firms”, and the least important is “to increase performance related pay”.

This latter reason merits further discussion. In Europe or US most governance failures and accounting scandals were heavily influenced by executive decisions to deceive investors with false information. Stock price appreciation and options´ values were at the core of these schemes, so it could be expected that respondents placed higher scores on this reason. The fact that they do not is eventually a sign of the low use of these mechanisms in the Portuguese corporate world.

No significant differences were found between the two samples in table 7.

Table 8 presents respondents’ opinions about the levels of consistency in applying accounting principles, from 1 (no consistency) to 7 (very high consistency).

Table 8. Perceived level of consistency in applying accounting principles

	Students (mean)	Professionals (mean)	Significant differences (Mann-Whitney test)
Historical cost	4,51	4,77	
Specialization of accounting periods	4,48	4,84	*
Materiality	4,31	4,35	
Substance over form	4,38	4,33	
Consistency	4,45	4,44	

Prudence	4,40	4,39	
Going "concern"	4,80	4,67	

(**) Significant at the 0,05 level

Only "historical cost" and "going concern" score higher than 4,5.

The difference between both groups in the "specialisation of accounting periods" can be related to differences observed in table 5. In the latter, professionals had higher scores on revenues, costs and accruals. The principle of specialisation has a strong influence in the recognition of these aggregates.

Table 9 presents respondents views on the need of reform in financial reporting rules (9.1) and the most important proposed reforms (9.2).

Table 9. Clues to reform financial reporting

Table 9.1."Do you think that financial reporting rules need to be reformed?"

	Yes	No
Students	73,0%	27,0%
Professionals	92,1%	7,9%

Table 9.2"State the four most important reforms you advocate to improve the quality of financial reporting"

	Students	Professionals
Higher penalties to managers that publish manipulated information	59	55
Higher penalties to accountants	39	20
Higher penalties to auditors	38	36
Introduce in Portugal the international accounting standards	36	39
A higher degree of precision in the Portuguese Accounting Rules (POC)	47	33
Reduce links between accountancy and taxation	16	28
To improve accountants' training	38	25
To compute profits on a cash flow basis	8	9

From table 9.1 it can be observed that professionals have a stronger opinion in favour of reform. This is probably due to the fact that, having experienced real life situations using or producing financial information, they have a more acute feeling of its shortcomings.

Table 9.2 presents solutions that respondents would propose to improve the quality of financial information.

Higher penalties for managers are the most favoured option. This is a sign that respondents feel that at the root of financial reporting problems are managers´ decisions. The harsher penalties for managers that Sarbanes-Oxley Act introduced seem to find favour with public perceptions of executive misbehaviour as a central factor in governance failures.

The second preferred option is, for students, a higher degree of precision in Portuguese accounting rules, and, for professionals, to introduce international accounting standards. Thus, the second favoured option of both groups is related to the rules that govern the production of financial information.

Two other results merit our attention. The first is the fact that although, in table 7, tax avoidance was seen as the main cause for manipulation of financial information, the reduction of links between taxation and accountancy is not a prime reform area. The second is the big difference in "higher penalties to accountants" importance of both groups.

The latter is an expected result: as some surveyed professionals have accounting related jobs, a self-defeating proposal could hardly been expected.

The former result is probably a sign that people do not have significant hopes of reducing links between accounting and corporate taxation.

Finally, table 10 presents evidence regarding perceptions about the quality of accounting systems in different countries.

Table 10. Perceived quality of accounting systems in different countries

	Students		Professionals		Significant differences (Mann-Whitney test)
	N	Mean	N	Mean	
Spain	79	4,37	67	4,25	
Russia	67	3,15	63	2,56	**
Germany	72	5,14	66	5,11	
Portugal	90	3,82	73	3,79	
Japan	71	4,99	65	4,88	
Brasil	71	3,00	68	2,68	
U.S.A.	84	4,13	67	4,57	
China	64	3,56	62	3,11	
France	76	4,83	66	4,76	
South Korea	64	3,62	62	3,52	

Mexico	63	2,78	64	2,50	
Australia	64	4,70	62	4,73	
Egypt	63	2,81	62	2,55	

(**) Significant at the 0,01 level

The first conclusion to draw is that some respondents did not feel comfortable with the question and did not answer. This factor was more common among students. From the 100 surveyed students, only in 4 countries (Portugal, USA, Spain and France) did more than 75 stated an opinion. For the 76 professionals, in every case more than 62

(81,5%) answered.

For students, the highest score is 5.14 (Germany) and the lowest is 2.78 (Mexico). Professionals also gave the highest score to Germany (5.11) and the lowest to Mexico (2.50).

There is a remarkable consensus between both groups. Two European countries (Germany and France), Japan and Australia stand out as the most appreciated accounting systems.

America, which tend to regard its accounting system as a model for the rest of the world, came after those 4 countries. Probably the accounting scandals that happened in the US affected the perception of the system´s quality.

Respondents are not very confident as far as the Portuguese accounting system is concerned. This is not surprising, given all the results shown in tables 2 to 9.

To sum up, it can be said that, in both samples, surveyed persons have quite different perceptions about the quality of financial information published by different types of firms; that external auditing is seem in a positive light as a way of improving the quality of financial reporting; notes to financial statements are seen as the most reliable source of financial information; balance sheet aggregates are more trusted than income statement ones; manipulation is seen as a pervasive situation so far as financial information is concerned; proposed reforms to improve financial reporting are advocated in the areas of penalties for managers who authorise publishing of manipulated information; and Germany, France, Australia and Japan have the most trusted accounting systems.

5. Perceptions of the quality of financial information and corporate governance: a conclusive note

Corporate governance is a ongoing process of setting up adequate mechanisms to solve conflicts that arise between different economic agents interested in firms' performance.

As such, good corporate governance is heavily dependent on the reliability of financial information. Data used for financial reporting are crucial for investors' assessment of a firm profitability and fund allocation. Managers' pay for performance schemes - be they related to accounting numbers or to stock market measures - are also strongly linked to the accuracy of financial reporting.

Lenders assessments of credit ratings are another area where published information is critical. And customers', suppliers' and public perceptions of a company's performance are highly influenced by its published financial information.

It is undoubtedly true that deterioration in the fairness of financial reporting is a severe blow to one of the cornerstones of good corporate governance.

If results presented in the previous section are representative of a global decrease in the reliability of financial information, then some changes should be made to restore lost confidence.

What is most striking is that students and professionals had a remarkable similarity of views. It is thus expected that students will go to the job market and make personal investment decisions with a pessimistic view of the quality of financial information.

Recent developments, like the Parmalat scandal, are also damaging factors to the perception of quality of financial reporting. Given that the present situation is not an ideal one, what changes could be promoted to restores some last hope?

Surveyed people produced two major lines of suggestions: increase penalties for wrong doing and make the accounting rules more suited to a better financial reporting. At a global level, it seems that authorities are moving in both directions.

Sarbanes - Oxley act in US and the increasing willingness of countries to adopt common accounting standards (accounting for goodwill is a good example) show that the crisis faced by financial reporting sparked action in some areas.

It remains to be seen if the momentum is not lost, and from the ruins of some of the worst ever cases of corporate governance it emerges a system better suited to the interests of society as a whole.

References

Bearle A, and Means G, 1932, *The modern corporation and private property,* Commerce Clearing House

Boatright , 1999, *Ethics in finance*, Blackwell

Burrough B and Helyar J, 1990, *Barbarians at the gate*, Random House

Bushman R and Smith A, 2002*, Financial accounting information and corporate governance,* Contemporary Accounting research, ed S Kothary *et al,* North Holland, p. 237-334

Cassidy J, 2002, *Dot.con,* Penguin Books

Chancelor E, 1999, *Devil take the hindmost,* MacMillan

Itner C et al, 1997, The choice of performance measures in annual bonus contracts, The Accounting Review, 72, p.387-399

Jensen M and Meckling W, 1976, Theory of the firm: managerial behaviour, agency costs, and ownership structure, In Jensen M and Smith C (eds) *The modern theory of corporate finance,* McGraw Hill

La Porta R *et al*, 1998, Law and finance, *Journal of Political economy,* 106, 1113-1155

Levitt A, 2002, *Take on the street,* Pantheon

Monks R. and Minow N., 2001, *Corporate governance,* Blackwell
Palepu K, 1986, Predicting take over targets, *Journal of Accounting and Economics,* 8, 1, p. 3-36
Schilit H, 1993, *Financial shenenigans,* McGraw Hill
Skinner D, 1994, Why do firms voluntarily disclose bad news?, *Journal of Accounting Research,* 32, 38-60
Sweeney A, 1994, Debt covenant violations and managers´ accounting responses, *Journal of Accounting and Economics,17, 3, p.281-308*

Filipe Coelho, Mário Augusto, Patrícia Moura e Sá, Arnaldo Coelho, Elsa Soares

THE EFFECTS OF ORGANIZATIONAL CULTURE ON SALESPERSON CUSTOMER ORIENTATION

Резюме

Известно, что организация может добиться успеха только при условии удовлетворения потребностей своих клиентов. Фактически, организационная работа в значительной степени зависит от понимания потребностей и требований клиента; необходимы исследования, демонстрирующие существование позитивной взаимосвязи между рыночной ориентацией (составляющей которой является ориентация на клиента) и работой организации в целом.

Особую важность для организаций представляет распространение собственной стратегии, ориентированной на клиента, среди своих сотрудников так, чтобы сотрудники разделяли эту стратегию и способствовали ее реализации.

В ходе исследований были выделены несколько важных результатов, относящихся к уровням ориентации на клиента сотрудников, работающих в сфере продаж. Такие сотрудники должны быть настроены на удовлетворение потребностей клиента, выполнение плана продаж и установление длительных отношений с клиентами.

В современных условиях наличие работников, ориентированных на удовлетворение потребностей клиента, важно для успешной деятельности любой организации; но для фирм, занимающихся предоставлением услуг – это основное условие успеха. Происходит реализация концепции маркетинга в организациях, оказывающих услуги. Ориентация на развитие и улучшение отношений с клиентами вызвала интерес к факторам, способствующим ориентированию продавца на потребности клиента (что до сих пор еще мало изучено). Поэтому целью статьи является дополнительное изучение рассмотренных определений и, в частности, изучение роли культуры организации.

В статье исследуются теоретические основы изучаемых вопросов, а также факторы воздействия концепции, ориентированной на клиента. Изучается роль организационной культуры на предприятии; удовлетворение от работы и обязательства работника по отношению к организации и выполнение продавцами их должностных обязанностей. Выдвигаются гипотезы, касающиеся связи организационной культуры и концепции, ориентированной на клиента. Рассматриваются данные тестирования выдвинутых гипотез на базе двух организаций, занимающихся предоставлением услуг; предлагаются результаты проведенного исследования.

INTRODUCTION

It is widely acknowledged that most organizations can only achieve success by satisfying their customers' needs. In fact, organisational performance is largely dependent upon the understanding of customer needs and requirements, with diverse studies demonstrating the existence of a positive relationship between market orientation, of which customer orientation is a component, and an organization's performance (e.g., Caruana, Ramasesham, and Ewing, 1997; Jaworski and Kohli, 1990; Narver and Slater, 1990; Baker and Sinkula, 1999). Of particular importance for organizations is how to disseminate their customer-oriented strategy to their employees so that these share the customer-oriented values of the firm and are inspired to carry out such strategy (Hartline, Maxham, and McKee, 2000). Several studies have already empirically identified several important outcomes of the level of customer orientation of salespeople, which has been positively related with customer satisfaction, the sales performance of salespeople and the development of long-term relationships with customers (Boles et al, 2001; Keilor, Parker and Pettijohn, 2000; Martin and Bush, 2003; Saxe and Weitz, 1982; Williams and Attaway, 1996). Hence, developing a customer orientated workforce plays an important role in any organisation, but for service firms it is particularly key. In fact, contact employees have been considered crucial in the implementation of the marketing concept in service organizations. This acknowledgement, spurred by the trend to develop better relationships with customers (Webster, 1992) has promoted the interest in understanding the organizational drivers of salespeople's customer orientation, about which little is still known (Boles et al, 2001; Brown et al, 2002; Flaherty, Dahlstrom and Skiner, 1999; Kennedy, Lassk and Goolsby, 2002). Hence, the goal of this study is to shed additional light on these determinants considering, in particular, the role of an organization's cultural traits.

This paper is organised as follows. Firstly, we review prior theory and research concerning the factors affecting salespeople's customer orientation and, in addition, we review the role of organizational culture on organizational performance along with the impact of role stress and job satisfaction and organizational commitment on salespeople performance. Next, we develop a set of hypotheses relating the cultural traits of the organization with salespeople's customer orientation. Subsequently, the hypotheses are tested in the context of two service organizations, and the results are discussed.

RESEARCH BACKGROUND

Customer orientation at the individual level can be understood as "the degree to which salespeople practice the marketing concept by trying to help their customers make purchase decisions that will satisfy customer needs" (Saxe and Weitz, 1982: 344). Similarly, Brown et al. (2002) suggest that customer orientation is the "employee's