

The Impact of Conditional and Unconditional Conservatism on the Earning Quality and Stock Prices

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Abstract: Conservative approaches can lead to incorrect matching of revenues and expenses so that decreases the stability of income items. The purpose of this paper is to examine the impact of conditional and unconditional conservatism on earnings' quality and stock prices in Tehran stock exchange and provide further insights on the effects of earnings' quality on stock prices. This study follows the asymmetric timeliness of earnings measure of Basu (1997) with further extension to measure the effect of conditional and unconditional on the quality of earnings and stock prices. This study employs cross sectional data analysis and multiple regression using data available for a sample of the largest 30 Iranian listed firms during the period of 2007 to 2013. The results suggest that (i) conditional conservatism negatively affects both earnings quality and stock prices of Iranian firms, and (ii) unconditional conservatism does not affect earnings quality but has a negative association with stock prices of Iranian firms. The findings of this study would help Iranian accounting standards setters to recommend accounting choices and policies that lead to high quality of earnings and provide financial reports that rationalize investors' decisions. It can be said that this study is the first to test the impact of both conditional and unconditional conservatism on earnings' quality and stock prices in Iranian setting.

Keywords: Conservatism, Conditional Conservatism, Unconditional Conservatism, Earnings' Quality, Stock Prices, Basu Model, Tehran Stock Exchange

1. INTRODUCTION

The quality of revenue items has an important effect on financial markets. Assessment of investors about the firms, useful predictions and stock purchasing decisions by the analysts are made based on revenue items. In recent years, the abuse of some large companies has been decrease the validity of such reports. Earnings with low quality, presents distorted information to the financial markets which mislead investors and other shareholders. As a result, understanding the nature of accounting transactions and different characteristics of the earnings quality is important.

Jinhan and zhang (2002), used the term of "earning quality" to refer to reported earnings. The earning with a high quality is a good indicator of future profits (Stable profits), thus while accounting perspective leads to unstable earnings that the quality is low. Experimental results indicates that if the companies follow conservative accounting constantly and without any commentary methods and accounting estimates some concerns about the earning quality will be created. Most of the previous research on the conservative approach is that this approach is the way to deal with uncertainty to protect creditors against unjustified distribution of the company's assets as dividends. Accounting conservatism, usually defined as a demonstrable difference to recognizing of benefits from losses. Watts (2003) states that the reasons of addressing to conservative approach, can be placed into three categories:

- The contractile incentives

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- Tax optimization
- Legal Risks

According Ball and Shivakumar's (2005) study, conditional and unconditional conservatism are defined as follows: Conditional conservatism means an application of methods and accounting policies that recognizes bad news more than good news in a time period. (Before event or related to news) and unconditional conservatism means taking some kind of accounting methods and policies that reduce the benefit and net book value of assets regardless of economic news (After events or independent of the news). Conditional conservatism means that the earnings of bad news will be recognized faster than good news. Previous studies have reported conflicting results on the effect of conservatism on earnings quality. Although this effect is positive in some studies (Zho, 2010) in other studies is negative.

Jinhan and Zhang (2002) Such results can be confusing to investors. For example, a company that adopts conservative accounting approach, will faced with the mismatch between current revenues and future expenses and the earning's stability will be reduced. Because Conservative accounting will affect for both the quality of items reported in the balance sheet and quality of reported earnings in the income statement. Earning value is recorded less than actual value. As a result unrecorded reserves have been achieved that provides the opportunity for managers to report higher profits in the future. According to gathered information, there is no comprehensive study about the simultaneous effect of conditional and unconditional conservatism on the earnings quality and stock prices in Iran. Therefore, this study is the first attempt to fill this gap in the literature related to the stock market.

However, this study is different with the mentioned previous studies of the many aspects ((Beaver & Rayan, 2005), (Lagor, 2008)). First this study survey the simultaneous effect of conditional and unconditional conservatism on the earnings quality and stock prices in Iran that it takes a new field. Second, in this study, the criterion of earning time asymmetry (Basu, 1997) were developed and added to the model. The ratio of operating cash flow to net income and ratio of market value to book value. Thus, the effect of conditional and unconditional conservatism on the earning quality and stock prices of a sample of Iranian companies is assessed.

In the past 20 years, the Financial Accounting Standards Board (FASB) in the United States of America has established standards for evaluation assets that has increased the tendency to conservatism in recent years. FASB Concepts Statement No. 2 FASB (1980) attempts to define conservatism as a prudent reaction to uncertainty which attempting to ensure that uncertainties and risks inherent in business situations are adequately considered. General description of accounting conservatism is mentioned by the International Accounting Standards Board (IASB) Suggests that conservatism is a degree of caution in the judgment inevitable practice for the required estimates in conditions of uncertainty so that the assets and revenues more than and liabilities and expenses not recognized less than the adequate value. Although there is no specific definition of conservatism, various definitions of the research is: For example, the first definition (Bliss & H. , 1924) that defined conservatism as "anticipate no profit, but anticipate all losses". Basu (1997) finds that conservatism is the reflecting of "bad news" earlier than "good news". (Givoly & Hayn, 2000) Define conservatism as a choice of some accounting principles that the revenue's slower recognition, faster recognition of the cost, the lower valuation of assets and the over valuation of liabilities, minimize the reported retained earnings. Nevertheless, conservative accounting can be divided into two different pairs of specialized vocabulary. For example, (Ball, The Global Financial Crisis and the Efficient Market Hypothesis: What Have We Learned?, 2000) classifies conservatism as an income and balance sheet conservatism. While the Pope & Walker (1999) refer to the two types of pre-event and post-event conservatism. Jander *et al.* (2004) point to the dependent of news and independent of news conservatism. Shivakumar and Ball (2005) use the terms of conditional and unconditional conservatism and this paper uses the same classification. Iran has a significant and considerable differences with developed markets. As

classified in the species growing accounting of the Middle East. An area that many cultural and social factors affected on the accounting policies and selections.

1.1. Background

Identification of profit components, which recently formed an important part of studies on the efficiency of the market began with Sloan study (1996). This approach, called the anomaly accruals on the assumption that the non-financial items of earnings (accruals) behaves differently than financial items (cash flow) in relation to sustainability benefits. If investors and users of financial statements have the ability to identify the differences in the behavior of the components of earnings, stated information will be absorbed by market immediately. Jinhua and Zhang (2002) define the earning quality in case of changing in conservative accounting over a period. Their hypothesis was that the differences between net assets reported with using of conservative accounting and net assets reported with lower using of conservative accounting equal to earning reserves. They found that defined degree of conservatism as the ratio of earning reserves to operating asset depends on the earning quality to changes in the degree of conservatism, over the time. Jinhua and Zhang (2002) empirically indicate that conservative accounting may lead to low quality earning and the stock market apparently sets a suitable price for low quality earning. The findings reveal that conservative accounting along with growth of investment, decreases profits and accounting rate of return and creates hidden reserves. In addition, decreasing in investment releases reserves and lead to higher rates of return and earnings. Beaver and Ryan (2005), investigated two kind of conservatism (definitive and conditional). Definitive conservatism is not affiliated to any economic news. For example, we can identify R & D costs as the secondary cost. Instead conditional conservatism is influenced by economic news. For example, it can be noted to the lower of Cost or Market rule, according to which, accountants reduces inventory value, when the cost of inventory is more than the market prices. But when the market price is lower, the cost will not increase. Based on these conceptions Ball *et al.* (2010) empirically show that the degree of conditional conservatism which is measured according to time difference in realizing bad news of earning compared to good news, is lower in companies with a definitive degree of conservatism, which is measured based on the ratio of stock price to book values. They have also designed a model that covers the different natures and interactions between conditional and unconditional conservatism. The results show that in unconditional accounting, due to the aspects of the predetermined accounting process, the net book value of the assets is underestimated. In conditional conservatism, when conditions is not appropriate, the book value is recorded at the low price, but in appropriate conditions is not recorded at the higher amounts. In addition, unconditional conservatism and other factors preempt Compared to conditional conservatism and thus impact on the earning's asymmetric reaction to positive and negative stock returns, both current and lagged. Jing (2007) investigated the relationship between earnings quality based on a set of six features such as the quality of non-cash accounts, consistency, psychological predictability, timeliness valuable connection and conservatism and the share prices. He also examines whether the relationship between earnings quality and the stock timeliness is stronger or weaker. The results show that earnings quality is important in the information development process. Zho (2010) examined the effects of conservative accounting on the share value. He found that there is a positive relationship between conservatism and the cumulative stock returns during the seasonal financial crisis. These results support this positive theory of accounting by providing evidence, that conservatism, is an efficient management mechanism that reduces the risk of information and controls agency problems and at last shareholders will benefit of that. Zho and Xia (2011) investigated the Chinese market reaction from the perspective of accounting conservatism during the reforms process. The results show that accounting information by the stock dividing reform in the China's securities market plays its role in the pricing of shares. In relation to this, completely in line with conservative accounting agencies and unusual cumulative returns, shows its affect for one day, three days, ten days and thirty days before and after the reopening day. The profitability of listed companies in the past, further improves the cooperative relationship between conservatism and market's reaction. Kurdistani and

Amirbeygi Langroodi (2008), used the earnings time asymmetry as a criterion for measuring the conservatism in financial reporting and examined the relationship of this criteria with the ratio of market to book value (MTB). The purpose of earning time asymmetry, in this study, refers to the definition of conservatism that whereby accountants tend to have a greater degree of verification to identify the good news of earnings to the bad news which leading to earning more timely reaction to bad news rather than reaction to good news. The results suggests a negative relationship between earnings time asymmetry and MTB as the two-evaluation criterion of conservatism. So that with increasing in the estimated period of earnings asymmetry criteria, this relationship becomes more negative. Reze Zadeh and Azad (2008) began to examine the relationship between information asymmetry and conservatism in financial reporting. To measure conservatism and information asymmetry, respectively domain of difference between the sales price and buying price of shares and Basu criteria was used. The results suggest that a significant positive correlation between information asymmetry of investors and the level of conservatism applied in the financial statements. Change in the information asymmetry between investors also cause changes in the level of conservatism. Khoshtinat and Yousefi aslin (2007) a similar study as "The relationship between symmetry and asymmetry of information with conservatism" reached to the same results. Limited resources have investigated the relationship between conditional and unconditional conservatism with the earning quality and stock prices. For example, Beaver and Ryan (2005) and Laguer (2008) were the first researchers that tested the effect of conditional and unconditional conservatism on the financial reporting. Hossein et al (2010) investigated the effect of accounting conservatism on the earning's stability and pricing coefficient. This study assumes that more conservative earnings are more unstable than the earning with a low level of conservatism. And also pricing coefficient in earnings with more conservatism is smaller than the pricing coefficient in earnings with less conservatism. Based on a sample of 88 firms listed in Tehran Stock Exchange and the period of (2012-1998), results show that earnings with more conservatism compare than earnings with less conservatism are more unstable. And pricing coefficients in the earnings with more conservatism are smaller than earnings with lower conservatism.

2. HYPOTHESES

This study, tests the effect of conditional and unconditional conservatism on earnings quality and stock price in the Tehran Stock Exchange. According to the theoretical foundations assumptions of the study are as follows:

- H1:** There is a significant relationship between earning quality and conditional conservatism
- H2:** There is a significant relationship between earning quality and unconditional conservatism
- H3:** There is a significant relationship between stock prices and conditional conservatism
- H4:** There is a significant relationship between stock prices and unconditional conservatism

2.1. Statistical Population

This study is based on data from a sample of 30 Iranian top companies announced by Tehran Stock Exchange. Due to the extent of the statistical community and specific problems arising from that and also due to some inconsistencies between community members in relation to the required data, the following conditions has been created for the selected the statistical sample and the research statistical sample, is selected by using of screening method:

- 1- Desired data for the years 2007 to 2013 is available
- 2- The companies that are listed on the Stock Exchange until the end of 2006 and also the name of the company in the period under review has not been removed from listed companies on the Tehran Stock Exchange.

- 3- Their stock trading is constantly done in Tehran Stock Exchange and not more than six months in each year of the trading halt.
- 4- Is not including investment companies (Holding) or specific activities (financing). It may be due to the nature of their activities, components examined in this study, is different for this kind of companies and may not be generalizable to the others.
- 5- Company have not changed the financial year during the period.
- 6- Financial year ending is on March 20.

2.2. Variables

This research is a descriptive study. Conditional and unconditional conservatism are the independent variable and the dependent variable is the earning quality and stock prices.

3. RESEARCH MODEL

There are many criteria that have been used for evaluating the degree of accounting conservatism in empirical research, to test theories and hypotheses related to conservatism. One of the interesting features of accounting conservatism resources is the lack of consistent results with a variety of criteria. Conservative criteria, which have been used and discussed widely in the literature include:

- Basu (1997) time asymmetry criterion
- Jinhua & Hain (2000) negative non-cash criterion
- Jinhua and zhang (2002) hidden reserves criterion
- Asymmetric ratio of cash flow to non-cash accounts by Ball & Shiva komar (2005)

Wang *et al.* (2008) analyzed previous studies about the conservatism to determine a criterion that has a widely used and concluded that Basu (1997) time asymmetry criterion is the dominant criterion in the majority of previous research conducted in this area.

Also in this study (AT) Basu (1997) time asymmetry criterion for testing hypothesis is used. Application of the Basu (1997) model can be explained on the basis that (i) this criterion, is the most commonly criterion of conservatism in the majority of previous studies. Previous research based on the standard AT, have been reached to the experimental results, which was coordinated with the anticipated results and confirmed the validity of this model. (iii) The model results can be used to explain the effect of adopting a conservative approach on stock prices and also finding potential relationship between stock prices and conditional conservatism.

Conditional conservatism is evaluated by using Basu (1997) regression model, Where earning and returns regression calculated and allowed that the return coefficient to be interpreted with the signal of return. Basu (1997) evaluates the conservatism according to reflect of bad news earlier than good news earning. Good news and bad news are determined based on stock return justice of the company (who represent the economic news). The basis of Basu criteria is that with the greater asymmetry, the degree of conservatism is higher. Time difference between good and bad news in the regression equation is shown by δ :

$$\frac{EPS_{it}}{P_{it}} = \delta_0 + \delta_1 DR_{it} + \delta_2 DR_{it} + \delta_3 DR_{it} * RET_{it} + \varepsilon_{it} \quad (1)$$

Where EPS is Earnings per share before extraordinary items for firm *i* in year *t*, P_{it} stock market initial price for firm *i* in year *t*, RET_{it} stock returns in year *t*, and DR_{it} is a dummy variable that equals one if RET_{it} be negative and zero otherwise. But Basu Criterion does not explain the effect of conservatism on the stock

prices. So aspect of criterion Will expanded to cover other variables. Theratio of Operating cash flow to net income (CFit 8 NIit) will be as a representative of the earning quality, to examine the effect of conservatism on earning quality. Thus the obtained criterion can be stated from the

Regression equation in the form below:

$$\frac{EPS_{it}}{P_{it}} = \delta_0 + \delta_1 DR_{it} + \delta_2 RET_{it} + \delta_3 DT_{it} * RET_{it} + \delta_4 CFO_{it} / NI_{it} + \varepsilon_{it} \quad (2)$$

The regression equation (2) is formed to evaluate the conditional conservatism and examine its relationship with the earning quality and stock prices. Hence by adding the ratio of market to book value (MTB)it is calculatedby dividing the market to book value of firm i in year t) and expansion of that, this model is used to assessing unconditional conservatism. Basu expanded version of the model can be expressed by the regression equation below:

$$\frac{EPS_{it}}{P_{it}} = \delta_0 + \delta_1 DR_{it} + \delta_2 RET_{it} + \delta_3 DR_{it} * RET_{it} + \delta_4 CFO_{it} / NI_{it} + \delta_5 MTB_{it} + \varepsilon_{it} \quad (3)$$

The basic model assumes that earnings of “bad news” reflects earlier than “good news”. According to Basu (1997) criterion,by increasing in the asymmetry of time, the company will be more conservative. By using Basu (1997) criterion regression of accounting earnings and stock returns (RETit) separately calculated for the good news and bad news of company for that year. A year might be considered good news for the company, which company’s stock return is positive or zero. And also a year might be considered bad news for the company, which company’s stock return is negative. The estimated slope coefficient shows that how embodied news in stock returns with respect to justice of news about earning have been detected. DRit dummy variable is used for separating the good news and the bad news and lets the slope coefficients to make a distinction between these two groups. It should be noted that δ_3 is the time asymmetry coefficient, and it is the main index of Basu’s criterion accounting conservatism. Which by increasing of thatthe degree of conditional conservatism will be higher. The study also,calculates the ratio of market to book value and dummy variable regression of stock returns for a period of five years. The estimated coefficient of the dummy variable for each firm represents a stable part of the difference between market value and book value of the company. With the higher level of ratio there is a more unconditional conservatism in the company.

3.1. Data Analysis and Discussion of Results

Table 1
Descriptive characteristics of variables

<i>SI</i>	<i>CF/I</i>	<i>MTB</i>	<i>E/P</i>	<i>Return</i>
MEAN	0. 581585	1249. 033	0. 259502	0. 229845
MEDIAN	0. 606462	198. 5143	0. 225273	0. 147
MAX	0. 996499	58965. 55	0. 878598	0. 62
MIN	0. 040548	0. 000000	0. 000748	-0. 21
SD	0. 166537	4452. 612	0. 172382	0. 271571
SKEWNESS	-0. 45445	7. 420399	0. 826098	-0. 086525
KURTOSIS	2. 877441	70. 64725	3. 444338	1. 799037
SUM	589. 1459	1265271	262. 8754	232. 833
Number of observations	240	240	240	240

As shown in Table 1 for all variables, distributional parameters are calculated separately. For example, the ratio of cash flow to revenue of 240 observations for 8 years respectively the minimum, maximum and average is equal to 0.040548, 0.996499, 0.5815853. Range of the variable distribution of data, covers from zero to 0.16, and therefore there is not a significant difference in the range of variations. Due to the positive coefficient of skewness, which is equal to -0.45445. It can be found that the skew distribution is to the left and there is a relationship (mean < median < mode). The kurtosis for this variable is equal to 2.877441, and indicates that the height and kurtosis for this variable is longer than the normal distribution. If the height distribution is more than the number 3, Show a longer kurtosis and if may be less than number 3, show the smaller kurtosis. In summary by increasing in the height and kurtosis of the variable, aggregation and data density is higher and vice versa. Given that the amount of statistic is equal to 2.877441 the height of distribution has not a significant different from the normal distribution and the height of data kurtosis is smaller.

Similarly, the values of the descriptive statistics of other variables can also be interpreted. In summary by comparing obtained results, it is clear that the most standard deviation related to market to book value. Therefore, we can say that differences and dispersion among all companies in terms of this variable, is more obvious. Similarly, the lowest standard deviation of the variable is the ratio of cash flow to revenue. Therefore, the performance of the companies in this variable, is approximately similar and dispersion is lower. Among the variables of the study, all variables except the ratio of cash flow to income and firm's return, the skew distribution is to the right. Relationship: (mean > median < mode). In this study, multiple regression has been used to assess the relationship between conditional and unconditional conservatism with earnings quality and stock prices.

To test the first and third hypothesis the following regression model is used:

$$\frac{EPS_{it}}{P_{it}} = \delta_0 + \delta_1 DR_{it} + \delta_2 RET_{it} + \delta_3 DT_{it} * RET_{it} + \delta_4 CFO_{it} / NI_{it} + \epsilon_{it}$$

Table 2
Least squares regression of the dependent variable of earnings quality to the price

Model components	β	Std. Error	T Statistic	Sig.
C	-0.79528	0.332899	-2.388955	0.0173
DR	-66528.95	29699.63	-2.24006	0.0256
RET	-0.229947	0.021595	-10.64803	0
DR*RET	0.005167	0.051539	2.100259	0.0202
CFO/NI	-1.62E-05	3.94E-06	-4.123132	0

Table 3
Significant test of the model

Durbin-Watson	Sig	Statistic F	Adjusted Coefficient	Coefficient of Determination
2.03182	0	36.18159	0.349682	0.359622

Table 2 suggests the results of the research model for the whole year about the first to third hypothesis. Due to the use of cross-sectional data, to eliminate the variance difference, generalized least squares method is used.

A) First, to determine the significance of the model, the T-test is used. Statistical assumptions of the test are as follows:

H_0 : All coefficients are zero

H_1 : At least one of the coefficient is not zero

- F statistics with regard to the amount of probability that is equal to (0.000), indicates that the related regression model above the 99% confidence is correct and the regression model is significant.
- B) After securing meaningful of estimated model, at the error level of $\alpha = 0.05$ t statistic is used to examine this relationship. As shown in table (4-7), the calculated probability of CFO / NI, DR * RET, RET at the confidence level of 95% and error of 5% is significant. (Level of significance is less than 5% and magnitude of t is greater than 2).
- C) The coefficient of determination (R) is a criterion that describes the strength of the relationship between the independent variables and the dependent variable. The value of this coefficient indicates that, the percentage of changes in the dependent variable explained by the independent variable. In this model, adjusted coefficient of determination is about 36%. It means that 36 percent of changes in the dependent variable can be explained by the independent variable.
- D) The amount of Durbin Watson statistic (DW) indicates the absence of serial autocorrelation problem. In other words, the Durbin Watson statistic is calculated for the regression model. The number is between (1.5, 2.5), which indicates the absence of correlation between variables.

As shown in table Correction coefficient according to the results described above, in the case of significance levels of t-statistics and F-statistic and given that the probability of the F-statistic is equal to (0.000), can be say that above the 99% confidence the model is correct. Results reveals that by increasing in earning time asymmetry (δ_3), the ratio of operating cash flow to net income will decrease. Thus, the first hypothesis is confirmed that the earnings quality is negatively associated with conditional conservatism. Which consistent with results of Jin Hau & Zhang (2002) and Ball & *et al.* (2013). The third hypothesis states that stock prices will decrease with the approach of conditional conservatism. Statistical analysis reveals that by increasing in time asymmetry (δ_3), stock prices will be lower. And thus, these results confirm the third hypothesis, according to which stock prices are negatively associated with conditional conservatism. Jing (2007) also report our results confirm that there is a negative correlation with the earnings quality and stock prices.

3.2. The second and fourth hypotheses testing

To test the third and fourth hypothesis, the following regression model is used:

Table 4
Least squares regression of the dependent variable of earning per share to price

<i>Model components</i>	β	<i>Std, Error</i>	<i>t- statistic</i>	<i>Sig</i>
DR	0.14326	0.099326	1.442321	0.1498
RET	10620.61	1817.885	5.842291	0.0000
DR*RET	-0.660706	0.049084	-13.46081	0.0000
CFO/NI	0.102917	0.017751	0.797643	0.129
M/B	0.003733	0.019926	0.187368	0.8514

Table 5
Significant test of the model

<i>Durbin-Watson</i>	<i>Sig</i>	<i>F-Statistic</i>	<i>Adjusted Coefficient</i>	<i>Coefficient of Determination</i>
1.956629	0	32.72702	0.2899	0.299037

Table 4 suggests the results of the research model for the whole year about the first to the seventh hypothesis. Due to the use of cross-sectional data, to eliminate the variance difference, generalized least squares method is used.

A) First, to determine the significance of the model, the T-test is used. Statistical assumptions of the test are as follows:

H_0 : All coefficients are zero

H_1 : At least one of the coefficient is not zero

F statistics with regard to the amount of probability that is equal to (0.000), indicates that the related regression model above the 99% confidence is correct and the regression model is significant.

B) After securing meaningful of estimated model, at the error level of $\alpha = 0.05$ t statistic is used to examine this relationship. As shown in table (4-7), the calculated probability of DR * RET, RET at the confidence level of 95% and error of 5% is significant. (Level of significance is less than 5% and magnitude of t is greater than 2).

C) The coefficient of determination (R) is a criterion that describes the strength of the relationship between the independent variables and the dependent variable. The value of this coefficient indicates that, the percentage of changes in the dependent variable explained by the independent variable. In this model, adjusted coefficient of determination is about 36%. It means that 36 percent of changes in the dependent variable can be explained by the independent variable.

Summary results of the first hypothesis

Summary results of the first hypothesis

<i>Hypothesis</i>	<i>Independent variable in the regression model</i>	<i>Dependent variable in the regression model</i>	<i>Results</i>
There is a significant relationship between earning quality and conditional conservatism	Earning quality	Conditional conservatism	Acceptance of the hypothesis. The above results with the results of Jinhan and Zhang (2002) and Ball <i>et al.</i> (2010) and the results of Tariq and Rash (2011) is compatible

Summary results of the Second hypothesis

<i>Hypothesis</i>	<i>Independent variable in the regression model</i>	<i>Dependent variable in the regression model</i>	<i>Results</i>
There is a significant relationship between earning quality and unconditional conservatism	Earning quality	Unconditional conservatism	Hypothesis is rejected. The result is compatible with Tariq and Rash (2011) results

Summary results of the Third hypothesis

<i>Hypothesis</i>	<i>Independent variable in the regression model</i>	<i>Dependent variable in the regression model</i>	<i>Results</i>
There is a significant relationship between stock prices and conditional conservatism	Stock prices	Conditional conservatism	Acceptance of the hypothesis. Jing (2007) also confirmed the above results and reports that there is a negative correlation with earning quality and stock prices.

Summary results of the fourth hypothesis

<i>Hypothesis</i>	<i>Independent variable in the regression model</i>	<i>Dependent variable in the regression model</i>	<i>Results</i>
There is a significant relationship between stock prices and unconditional conservatism	Stock prices	Unconditional conservatism	Hypothesis is rejected. The result is compatible with Tariq and Rash (2011) results.

D) The amount of Durbin Watson statistic (DW) indicates the absence of serial autocorrelation problem. In other words, the Durbin Watson statistic is calculated for the regression model. The number is between (1.5, 2.5), which indicates the absence of correlation between variables.

As shown in table 5, Correction coefficient according to the results that described above, in the case of significance levels of t-statistics and F-statistic and given that the probability of the F-statistic is equal to (0.000), which can be say above the 99% confidence the model is correct.

The second hypothesis refers to the impact of unconditional conservatism and is expected to lead to an increase in the earning quality. Statistical analysis shows that the relationship between the market to book value as a criterion of unconditional conservatism, and the ratio of operating cash flow of unconditional conservatism, has not impact on earning quality and the second hypothesis is rejected.

The fourth hypothesis refers to the expected positive relationship between stock prices and unconditional conservatism. The results show that there is a significant negative relationship between stock prices and conditional conservatism, among companies that have adopted the unconditional conservatism. In fact, turning to the policy of unconditional conservatism has a negative impact on stock prices. And so the fourth hypothesis is rejected. It should be noted that the above results is consistent with the results of Tariq and Rash (2011).

This study evaluates the effect of conditional and unconditional conservatism on the quality of reported earnings in financial statements and the stock prices of a sample of companies listed on Tehran Stock Exchange. In relatively dynamic markets such as Iran, stock returns simultaneously and quickly reflects all publicly available news. The timeliness of earning for bad news means that is more Susceptible to negative rather than positive returns. As the slope coefficients and (R^2) regression of earning to return also shows. In the growing market of Iran, the results show that conditional conservatism, earnings sensitivity to negative returns of 4.89 times greater than the sensitivity of earnings to positive returns. The main results of this study for a sample of Iranian companies have been recorded as follows:

- (i) All of the studied companies, follow the conservative accounting policies and procedures such as cost, or below market value for assessment inventory, recognition of losses for assets, certain values and tangible costs, including research and development, advertising and quickly depreciation method.
- (ii) Earnings quality and stock prices are negatively associated with conditional conservatism.
- (iii) There is no significant relationship between earnings quality and unconditional conservatism.
- (iv) There is a significant relationship between earnings quality and unconditional conservatism.

3.2. Limitations

Like other studies, this study also has limitations. First the survey results, limits the decision makers, because it cannot be claimed that the sample is representative of all Iranian companies stock. Second, the model is used to evaluate both the conditional and unconditional conservatism, is not founded based on described criterion of this two types of conservatism. Jiu Li and *et al* (2007) found that Basu (1997) criteria may not be suitable due to some limitations to all areas of research. For example, they found that the

characteristics of firm information environment that is not associated with conservatism, can be affected on the Basu (1997) criterion. In addition, they concluded Basu criterion with other measures of conservatism has a negative correlation.

3.3. Suggestions for Future Research

1. Under the rules of the stock exchange, listed companies are required to follow rules. According to the results of the research that has been done to the companies listed on the Stock Exchange. To evaluate impact of the above measures, on the Earnings quality, it is recommended, that the hypotheses of this study be tested for non-stock corporations.
2. It is recommended to researchers, in a separate study, examine the relationship between levels of conservatism.

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