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THE ROLE OF REPLACING FAIR VALUE ACCOUNTING WITH THE PRINCIPLE OF HISTORICAL COST IN ENHANCING THE QUALITY OF ACCOUNTING INFORMATION

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Abstract: *This study aims to show the disadvantages of adopting the principle of historical cost, and its impact on reducing the quality of accounting information, and the necessity of applying fair value accounting and its role in enhancing such information. It is well known that the usefulness of accounting information is measured by the extent of its usefulness to various communities of users, and by its high quality manifested by its appropriateness and reliability. Based on this, the study shows that the application of fair value accounting enhances the quality of accounting information. The researcher has adopted the deductive approach based on logical thinking in answering the main question of this study, and the research has come to the conclusion that fair value accounting plays an important role in increasing the quality of accounting information embodied in the enhancement of appropriateness and reliability. The study recommends the necessity of modifying the accounting conceptual framework and replacing fair value accounting with the principle of historical cost. It also recommends the necessity of adopting this approach by the professional accounting organizations worldwide.*

Keywords*: Fair Value Accounting, Historical Cost, Quality of Accounting Information, Appropriateness, Reliability.*

1. INTRODUCTION

The quality of accounting information depends on the relevance and reliability of this information. It is also influenced to large extent by the measurement basis in effect. The accounting literature used to rely heavily on the historical cost principle to measure different items in the financial statements. However, developments over time have proven the inability of historical cost principle to maintain the relevance and reliability of accounting information. The need of new basses which avoid the shortcomings of the historical cost principle motivated the movement of both researchers and accounting governing bodies toward fair value accounting.

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2. STUDY'S PROBLEM AND QUESTIONS

Although the continuous interest of different users in getting high quality financial information for decision making purposes, the use of historical cost principle reduces the quality of this information and hence its reliability. Consequently, to address this issue, an alternative principle was introduced, which is the fair value accounting. The study problem arises from the replacement of historical cost principle with fair value accounting and can be expressed in the following main question:

Does the application of fair value accounting enhance the quality of accounting information?

Two sub questions can be derived from the main question:

- Does the fair value accounting reinforce the relevance of accounting information?
- Does the fair value accounting reinforce the reliability of accounting information?

3. SIGNIFICANCE OF THE STUDY

The novelty of this paper arises from its emphasis of replacing historical cost accounting with fair value accounting. It shows how this shift would enhance the quality of accounting information of the financial statements which represents the basis of the investment decisions of different parties involved.

4. STUDY OBJECTIVES

- To describe the historical cost principle and describe its shortcomings.
- To describe fair value accounting, and to justify its use in practice.
- To explain how the replacement of the historical cost principle with fair value accounting would enhance the quality of accounting information.

5. PREVIOUS STUDIES

Christensen and Nikolaev (2013): This paper investigates the choice of historical cost versus fair value accounting for nonfinancial assets in an environment governed by market forces rather than regulations. Their authors indicate a very limited use of fair value accounting especially when it is hard to establish reliable estimates of the fair at a reasonable cost (for example, plants and equipment).

Alnajjar, H. J. (2013): This paper investigates the impact of the application of fair value accounting on the reliability and relevance of the accounting information in the financial statements of Palestinian corporations, and describes the problems

facing these companies in the application of this principle. It includes a survey of the external auditors and the financial managers of Palestinian corporations. The study presents two main conclusions. First, the application of fair value accounting does increase the relevance and reliability of the financial statements information. Second, there are several challenges facing the application of fair value accounting, including the unavailability of an effective asset markets to establish the fair value for different assets in Palestine. The author strongly recommends that the supervising bodies should increase the efficiency of Palestinian asset markets to enable these markets to establish prices that truly reflect the fair values of the assets.

Frajj, M. H. (2012): This paper discusses the standards that address fair value accounting (including international accounting standards, American accounting standards, and Egyptian accounting standards) to demonstrate the qualities fair value adds to accounting information. The main results show that financial data is more useful for its users when it is measured on the basis of fair value rather than historical cost, and that the use of fair value increases the quality of accounting information. The author, hence, recommends that the management should encourage the accountants to apply the international accounting standards related to fair value.

Al-Melyjji, H. H. and D. A. Kareema (2012): This paper inspects the accuracy of accounting estimates under fair value accounting. It discusses the tendency of accounting standards board's toward the use of fair value in measurement and the advantages and drawbacks of this application. The study points out several results. First, the reliance on fair value accounting allows for a suitable and realistic measurement and disclosure of different assets and liabilities. Furthermore, the publication of information measured on the basis of fair value allows for more realistic and suitable estimations of the future profits and cash flows, creates a kind of transparency, and increases the confidence of the financial statements users and hence reflects positively on share prices.

Al-Abadi, M. R. (2010): This paper describes the accounting measurement bases in the Saudi and the international accounting standards, reviews the status of fair value accounting in both sets of standards, and emphasizes the importance of developing the Saudi accounting standards by adopting fair value measurements and disclosure. The paper indicates that there is a gap between Saudi and the international accounting standards in several aspects. First, contrary to international standards which consider the fair value the rule and the historical value the exception, Saudi standards make a minor use of fair value principle which is only used for explanatory purposes in the financial statements. Moreover, unlike international auditing standards, Saudi auditing standards lack any equivalents

of the auditing fair value measurements and disclosures standard (ISA545) and the accounting estimates standard (ISA540). The author recommends developing Saudi accounting standards to by adopting fair value measurements and disclosure, and developing Saudi auditing standards in line with international standards. He highlights the importance of including explanatory instructions for the auditors the address the challenges arose from measurement and disclosure based on fair value.

Al-Kashi and Al-Khateeb (2004): This papers investigates the reasons of the tendency of accounting standards board's toward fair value and economic income, discusses the accounting standards of fair value and economic income and their advantages and drawbacks, the challenges facing the application of these standards, and the implications for the economy. The paper specifies several interesting results. First, the absence of active markets for several assets means that companies would turn to the internal valuation, and, hence, increases investors' concerns about the manipulation of accounting information. Additionally, it is inefficient to apply international standards (based on fair value accounting) in the developing countries because of the high cost associated with this application from the companies' point of view.

6. METHODOLOGY

To serve the study objectives, to reach the best understanding of the impact of the application of fair value accounting on the quality of accounting information, and to answer the study questions, the researcher employs a mixed approach that uses the inductive methodology -which relies on reasoning- and the deductive methodology which starts from basic facts to find the connections between the different aspects of the accounting information quality and fair value accounting. Additionally, the research surveys the past literature on the historical cost principle, fair value accounting, and the quality of accounting information.

7. THEORETICAL FRAMEWORK

7.1. The Historical Cost Principle

The historical cost principle is considered one of the oldest and most important accounting principles that govern the construction of financial statements. It is used to measure and valuate the fixed assets, liabilities, finance sources, expenses and revenues on the basis of the historical cost of purchase or production. It ignores the changes in the purchasing power of money especially during inflationary or deflationary periods. Although there are many definitions of the historical cost, all of these definitions provide the same meaning. For example Kieso et al. define

the historical cost as the "the price or cost of an asset or liability when it is realized or purchased, and is used to measure most assets and liabilities". Additionally, the American Institute of Certified Public Accountants (AICPA) defines the historical cost as "the monetary values of the cash payments, other assets, equity shares, the services provided, or the liabilities created in connection with the reception of goods and services form other parties". (Al-Haialy & Al-Asadi, 2008).

7.1.1. The Justifications of Historical Cost Basis

The justifications of the historical cost principle include the following (Abdullah, 1983):

1) It is possible to verify historical cost data. This increases the degree of objectivity and hence the reliability of accounting data. The researcher argues that the most important feature in this context is that it allows for comparisons.
2) The historical basis is consistent with several components of the financial accounting theoretical frame work. This includes:
    a) Revenue realization principle which states in it classical form those changes in the values of assets and liabilities cannot be recorded until they are realized through transactions.
    b) Matching principle which states the income is determined by deducting the expenses of a given period from the revenues of the period, not by comparing the value of net assets in the end of the period to their value in the beginning of the period.
    c) Continuity which assumes that a project or an entity would last in the 12 month following the last balance sheet. The going values of assets are not to be used unless the entity went into liquidation.
    d) Consistency principle. The historical cost basis states that assets and liabilities have to be valued at cost regardless of any changes in the prices.
    e) One of the financial accounting restrictions is the prudence policy or principle which indicates that increases in asset prices should be ignored to make a reasonable picture of the financial position.
    f) Monetary unit assumption which states that recording must be in the original monetary units ignoring any changes in money value due to inflation or deflation.
    g) Actual measurement principle which states that recoding in books and financial statements must reflect what really happened not virtual circumstances.

7.1.2. Criticisms of Historical Cost Principle: (Jarboua (2001))

1) The matching between the revenues which are measured using going prices and the expenses which are measure on the basis of historical values would mix the profit (loss) from operations with that realized from changes in input prices. The profit (loss) from operations should be calculated by subtracting the expenses in current prices form revenues in current prices. Meanwhile, the gain form speculation on input prices changes should be calculated by subtracting the expenses in historical prices from the expenses in current prices.

2) The delay in declaring the changes in asset and liabilities prices until they are realized through transactions will cause overlaps between different accounting periods which contradict with period independence principle. In other words, the profit in an accounting period will reflect the consequences of past economic developments that have not realized until the current period. Also, the current profit will not reflect the consequences of all developments in the current period since some of these will realize in future periods.

3) The reliance on historical cost basis would drop several intangible assets from the financial statements, since they there are no transactions related to these assets. Examples include goodwill, human capital, monopolistic privileges, and the information system of the entity and other intangible items.

4) The reliance on the historical cost basis means ignoring changes in the value of the original monetary units. There are some accounting approaches that suggest replacing the original money units with money units with fixed purchasing power. These approaches are justified by the fact that the incorporation of purchasing power changes is a diversion from historical cost principle since the correct application of this principle requires the usage of homogenous measurement units for all items in the balance sheet. Moreover, ignoring the changes in price level would make grossing and netting the items in the balance sheet impractical (White and Sami, 1994).

5) The reliance on the historical cost basis when there are significant changes in the going prices of different assets and liabilities make the book values far away from representing the current values. This would decrease the usability of financial statements. Hence, the application of the principle includes an ignorance of the economic principle of establishment theory which makes the accounting model unable to depict the economic facts and to serve the decision makers especially when it comes to the estimation of the future cash flows.

7.2. Fair Value

No one argues that the fair value principle shifted accounting theory into new horizons, and created a comprehensive change in the structure and implications of accounting data. This was a result of the development in accounting theory during the past three decades which reflected in the international accounting and financial reporting standards. Saleh (2009) defined the fair value of an asset as "the amount at which the asset can be purchased or sold in an actual transaction between informed parties who are willing to transact in normal circumstances (no liquation looming)". On the other hand, the fair value of a liability is "the amount that is paid in an actual transaction between informed parties who are willing to transact in normal circumstances (no liquation looming)". The fair value can be determined using bid or offer prices, or estimated in the absence of such prices. The Financial Accounting Standards Board justified the use of the term "fair value" by the absence of established market prices for all assets and liabilities (Barth, 2004). The American accounting Standard 107 defines the fair value as "the transactional value of an asset in an actual transaction between parties who are willing to transact in normal circumstances (no liquation looming or fire sales)".

The International Accounting Standards Board defines the fair value as "the amount at which an asset can be sold or a liability can be paid back, between informed parties who are willing to transact on a pure commercial basis". This definition appears in several standards such as Standard 32 Paragraph (5), Standard 36 and Standard 39. Standard 40 indicates that the fair value is determined in a specific date and changes from time to another depending on market conditions.

The international financial reporting standards of 2009 state that the fair value is the transactional value of an asset traded between informed parties who are willing to transact and in their free will. Humaidat (2004) defines the fair value as "the value at an asset can be sold or a liability can be paid back between parties who are willing to transact and reasonably informed. Al-Saafeen (2005) defines the fair value as "the amount at which an asset can be sold or a liability can be paid back, between two informed parties who are willing to transact and with no common interests".

Based on above, the research concludes that all the definitions emphasize the following points:

1) The independent of the parties and the ability to bargain.
2) The transaction must be in normal circumstances.
3) The desire to transact of the different parties.
4) The same set of information must be available for different parties.

7.2.1. Why Should Fair Value Be Used?

a) Investors concentrate on the relevance property of information to make proper decisions. Relevant information is the one that is measured on the basis of fair value rather than historical cost (Quaderi, 2010).

b) It is considered an efficient measure especially for share and bond prices.

c) It is related to the concept of physical capital protection, which represents the best measure of performance.

d) It is related to the comprehensive income concept which is more useful for the users of financial statements.

e) It helps in enhancing the financial analysis through providing ratios that reflect reality (Boxani *et al.*, 2010).

Alnajjar (2013) indicates that the use of fair value accounting is a better alternative that addresses the shortcomings of the historical cost principle and enhances the quality of produced data. He points out the following advantages of the fair value accounting:

a) Fair value reflects the actual conditions of the establishment and it makes the financial statements give a better representation of the true financial position, activity results, cash flows and changes in net worth.

b) If the values assets and liabilities are estimated on the basis of fair value, they will reflect the economic income since market prices are taken into account.

c) It is consistent with the concept of physical capital protection.

d) This approach provides an accurate measure of value and economic profit.

e) Fair value accounting takes the changes in the purchasing power of money into consideration.

f) The use of fair value standard is more suitable for decision making and financial analysis, and a better basis to estimate activity results and cash flows.

g) The information produced on the basis of fair value allows for comparison between similar businesses that use fair value accounting.

h) Fair value provides insights about the future to the investors.

7.2.3. The Criticisms and Drawbacks of Fair Value

Despite of the advantages, fair value has not provided a complete system that allows for financial declaration, measurement and disclosure. Hence, it has received

several criticisms on the basis of unsuitability. The most important criticisms include (Khouery, 2006; Geara, 2012):

1) The measurement of fair value includes a big deal of personal judgment and bias, never mind the use of contradicting measurement basses.
2) There are many investments which do not have an established market price and their measurement relies on historical cost.
3) The application of fair value accounting in the context of investment is complicated and uses different measurement methods some of which is related the desire of the business to sustain investments and the other is related to fair value estimation.
4) Different analysts deliver different estimates decreasing the reliability and accuracy of the estimates.
5) Estimation costs may exceed the potential benefits.

The researcher argues that these criticisms do not reduce the importance of fair value accounting. It is possible to reduce bias through determining the methods of fair value measurement under different circumstances. The reliance on professional estimation and analysis agencies -that have no stake to avoid conflict of interest- may help in constructing fair and unbiased estimates.

In the case of investments that have no established market prices, it is possible to use it current cost as an estimate of its fair value instead of the historical (old) cost. For investment, the purpose of the investment can be easily determined whether it is control or speculation, then a decision about which valuation method (fair value or historical cost) to be used can be made. The determination of fair value would not be different whether the value is estimated for a single asset, a group of assets, or the business as whole.

For the issue of cost-benefit, the researcher sees that the required information is available in most cases at no extra cost. Additionally, estimation and analysis agencies would not unreasonable exaggerate their fees since they might lose their customers doing so.

In any case, the researcher argues that every approach would have advantages and drawbacks and that the comparison between these should decide whether this approach would be used or not. There is no doubt that the advantages of the application of fair value accounting outweigh its shortcomings.

7.3. The Quality of Accounting Information

Generally, the main objective of accounting is to produce and deliver useful information for decision making. In other words, the benefit of information is

the basis from which accounting starts. Financial accounting specializes in providing information that helps in rationalizing the decision making within the establishment, and is important for current and perspective investors (Hanaan, 2009). The quality of accounting information is determined by whether this information meets the characteristics of useful accounting information or the fundamental rules that are used to judge the quality of accounting information. Determining these properties or characteristics helps the supervising bodies, when setting the accounting standards. It also helps accountants, when preparing the financial statements, in evaluating accounting information under alternative approaches and in differentiating between important and unimportant clarifications (Al-Jadi and Al-Hajj, 2010). Usually, accounting literature distinguishes between two sorts of characteristics. The first is related to decision makers, whereas the other is related to information itself and includes primary and secondary characteristics that have some determinants and restrictions. In the following section, these characteristics are described in details.

7.3.1. The Characteristics Related to Decision Makers or Accounting Information Users

To give a fair judgment on accounting information, the decision maker who is using this information must have a set of characteristics. These characteristics include (Al-Kadi and Abo Zalta (2010):

a) The ability to understand information content.

b) The ability to correctly use the information in the suitable and relevant decisions, for which is information was produced.

c) Qualitative and time experience in dealing with accounting information in the past.

Therefore, the right use of accounting information requires a proper decision maker who is prepared to effectively use this information. In other words, the use of accounting information by a person who does not have a minimum level of understanding of the meaning of this information would not make sense.

7.3.2. The Qualitative Characteristics of Accounting Information

What meant here is the characteristics or properties accounting information, presented in the financial statements, should have to become of a higher quality and more useful for decision makers (Al-Shami, 2009). This includes two primary and two secondary characteristics.

7.3.2.1. The Primary Characteristics

A. Relevance Property: The relevance property is considered one of the main qualitative characteristics of accounting information; to be useful, accounting information must be relevant and suitable for the needs of decision makers. Accounting information has this relevance property when it affects the economic decisions of the users by allowing them to evaluate the past and anticipated developments. FASB defined relevant information as "the information that is able to make differences in decisions through helping the users in developing estimation of future results, and reinforce or correct the past estimations. Information can be relevant by influencing understanding, objectives, and decisions (Homaidi, 2009). Basheer (2006) indicates that "relevance means the presence of a relationship between financial accounting information and the purposes for which this information is prepared". "Information would be relevant if it helped the decision maker in evaluating the outcome of an alternative, given that other characteristics of useful information are met". Fattouh et al. (2006) defined relevance as "The ability of accounting information to change or influence the decision of its user. In other words, it is the ability of information to influence decision making". It can be noticed that all the above definitions agreed on the influence of information on the decision maker and on the principles of full disclosure and relative importance. The relevance property enables information users to:

- Build estimates for the consequences of past, present and future developments.
- Reinforce or change a current expectation, which means that relevance affects the degree of uncertainty of the decisions being made.
- Enhance the ability of making estimations about the future results and correct previous estimates.

To achieve information relevance, three sub characteristics must exist. This includes the ability to estimate future outcomes, the possibility of feedback evaluation, and synchronization (Al-Sheerazi (1990)).

1) The suitable timing of information, this means providing the information in the right time before it lose its benefits or ability to influence decision making (Hanaan, 2009). This is what Al-Sheerazi (1990) called synchronization. It is axiomatic to say that providing information when the need to it ends makes it useless for decision making and hence irrelevant.
2) The ability to estimate future: this means that accounting information has to be useful when future-related decisions are made Khamkani and Swaisi, 2011). This is what Al-Sheerazi (1990) called the estimating power of information.

3) When the user exercises a kind of estimation when making a decision about the future, relevant information is this that allows for better estimations.
4) The possibility of feedback evaluation: This means that accounting information can be used for evaluation and control purposes through feedback and address the problems arose from misuse or inefficiency .

Fattouh *et al.* (2006) indicate that "accounting information that are produced by the accounting system must able to provide the user with the ability to make comparisons between past incidents and to adjust for changing environmental conditions, and hence the ability to evaluate the decisions that were based on expectations and to correct deviations had they happened".

B. Reliability Property: This property is related to the degree of confidence the user has in accounting information to be used in making decisions. According to Hamadeh (2010), reliability means "that measurement and disclosure methods that were chosen to produce and present the results would be suitable for the surrounding environment, that these methods were applied in a way that allows other users to reapply them to check the outcomes, and that information provided reflect the developments it is describing without any significant bias as it should be objective information can be relied on. The reliability of accounting information increases its usefulness". To maintain reliability, information must have three sub properties including verifiability, representational faithfulness, and neutrality (Schroeder (2010)). Similar description is given by Al-Sheerazi (1990) who indicates three sub characteristics: faithfulness in representing the incidents, verifiability, and information neutrality.

1) Faithfulness in Representation: Faithfulness in representation means that accounting information is able to correctly and faithfully reflect the related incidents without any manipulation or bias. Al-Seerazi (1990) specifies that faithfulness in representation means the presence of high degree of matching between the measurements (information) and the measured values. This does not necessarily means that information must be certain or completely accurate. The reality might require showing the probability distributions and the error term of the values that appear in the financial statements. Schroeder, (2010) indicates that faithfulness in representation refers to the agreement and consistency between accounting figures and the incidents described by this information. Yet, increasing consistency does not necessarily guarantee that accounting measurements would be suitable for the needs of the user if the incidents represented by these measurements are not suitable for the purpose of the user. Maintaining faithfulness in representation requires the avoidance of two kinds of bias:

- Measurement bias: such as the bias when historical cost and prudent principle are employed.
- Measurer bias: which might be intentional (if the measure is dishonest) or unintentional because of the lack of knowledge or experience (Al-Sheerazi (1990)).

2) Neutrality: According to neutrality means "when developing or applying standards, the concentration should be focused on information relevance and reliability, not on the implications of a rule for a specific party. The neutral choice between alternatives must be unbiased and must not lead to predetermined results, since it is not possible to find predetermined results that serve several different interests of the several users of financial statements information".Al-Sheerazi (1990) demonstrates that neutrality is important on two different levels:

The first level is the governing bodies that are responsible of organizing accounting practices, especially those setting accounting standards. Here neutrality means non-bias or toward a predetermined result of specific practice. This makes neutrality almost impossible to attain. Hence, neutrality here is relative and means the independence of the system of any presumption of the objectives of financial statements users' as much as possible (Al-Sheerazi, 1990).

The second level is the accountant responsible of producing financial statements. Here neutrality means avoiding the intentional bias of the accountant in producing or presenting accounting information to reach predetermined results or to direct the information user in a specific direction.

3) Verifiability: Verifiability means the possibility of producing similar results by different persons, given that the same measurement methods were used. Verifiability is sometimes described as an equivalent of objectivity, and, according to Al-Sheerazi (1990), it is the term that is currently used in accounting literature to refer to objectivity, which is a requirement of any scientific research. Schroeder (2010) indicates that "verifiability can be maintained through ensuring high degree of consistency between different measures that use the same measurement methods".

7.3.2.2. Secondary Characteristics

The interaction between the two primary properties (relevance and reliability) produced secondary properties of accounting information. Al-Kadi and Abo Zalta (2010) described the following secondary characteristics.

A. Consistency Property: This includes the application of the same accounting procedures for similar incidents in different periods, and the application of the same principles, measurement methods, and procedures for all financial statements

items. It means continuing the use of the same methods used in measuring and delivering accounting information from one period to another. If a change is needed, it should be mentioned clearly so the user can take it into consideration. It also means that economic activities should be recorded and disclosed in every financial period. Consistency includes (Helwa Hanaan (2009)):

- The application of the same accounting procedures for similar incidents in different periods.
- The application of the same principles, measurement methods, and procedures for all financial statements items.

B. Similarity and Comparability: This means that accounting information is allows for comparisons across time for the same entity and between an entity and another in the same industry. The presentation of accounting information, in a way that enables external comparisons with the information from other entities in the industry or internal comparisons inside the entity, increases the ability to measure performance, to produce improved estimations, and to rationalize decisions (Fattouh et al., 2006). To be comparable, accounting information requires two main elements:

- The similarity of the methods used in the production of financial data in terms of measurement and disclosure.
- Consistency, which means that similar bases and principles must be followed in different periods in terms of measurement and disclosure to make the published financial data comparable.

7.3.3. Similarity is vital for accounting information to be comparable

Restrictions on the Qualitative Characteristics of Accounting Information. In addition to the qualitative characteristics of accounting information, FASB set to main restrictions on qualitative characteristics of accounting information (Fattouh *et al.,* 2006).

A. Cost and Benefit: The production of accounting information requires several costs. Hence, a comparison between these costs and the benefits of the production and use of accounting information. The management decision about the production of accounting information would go through if the benefits are at least equal to the cost. This restriction represents a fundamental standard in the evaluation of accounting system efficiency in providing information (Fattouh *et al.,* 2006). It is important to understand the cost of information increases in a geometric sequence when more information is to be collected about a specific issue. The management has to balance between costs and benefits. The expected return from the use of accounting information can be measured using several methods

including the expected value of the extra information which the difference between the return expected from the extra information and that expected form normal information.

B. Relative Importance: This restriction determines the level and degree of relative importance of accounting information from the users' point of view. It indicates that information in financial statements needs to be classified and categorized according to the relative importance from the perspective of the users. It also emphasizes on the importance of focusing on the content of the information rather than the form (Fattouh et al., 2006). Accounting information would be of high importance if its omission leads to significant impact on decisions.

8. THE INDUCTIVE-DEDUCTIVE ANALYSIS TO ANSWER STUDY QUESTIONS:

The researcher starts by discussing and analyzing the sub questions then moves to the main question.

8.1. First Sub Question: Does the fair value accounting reinforce the relevance of accounting information?

As the theoretical framework described, the relevance of accounting information relies on its ability in influencing the decisions or their directions. It is reasonable to say that the historical cost (of an asset for example), which reflects an old cost that does not reflect the current situation, cannot provide relevant information. The alternative would be a value that reflects the going value of the replacement cost of the asset. Fair value is the suitable alternative since it can influence the decision maker by reinforcing or making decisions. Turning to the components of the relevance property, the research presents the following:

(a) Synchronization: The usage of historical cost can be justified by the availability of information when needed by the user in contrast to fair value basis. A possible response to this point would be that the early planning induces information users to search for the information well before it is needed. Additionally, it is possible to certify estimation and valuation agencies in a fashion that is similar to auditing and financial analysis and consultancy agencies, and under certain regulations that regulate and organize the activities of such agencies. The databases of such agencies would provide a ready data source that can be used when fair value estimations are needed. This would make information based on the fair value basis ready and available in the right time. Hence, the researcher argues that synchronization would not cause a problem when turning into fair value accounting.

(b) **The ability to estimate future:** The historical cost is not useful at all in estimating the behavior and development of an item in the future. It often needs modifications on different bases, such as the general price level, to be used for estimation purposes. Hence the researcher concludes that instead of developing bases to enhance the historical cost, some of which may rely on judgments with no scientific or practical foundations, it is better to use fair value with clear scientific or practical foundations.

(c) **Feedback:** What mentioned in the previous section applies to this section. The reliance on fair value makes the feedback evaluation more useful because of the homogeneity between the estimated values and the actual value, and hence makes the valuation more objective.

The above discussions of relevance property components support the research's view in the beginning of the analysis of this feature. Hence they assign a positive answer to the first sub question: the fair value accounting does reinforce the relevance of accounting information.

8.2. Second Sub Question: Does the fair value accounting reinforce the reliability of accounting information?

This question looks problematic. The proponents of historical cost principle insist on the reliability to prove the importance of attaining the historical cost as it produce absolutely credible information in contrary to fair value. The researcher argues:

(a) The regulation and supervision of estimation and valuation agencies and holding them for any possible damages caused by their projections, to the extent of criminalizing their wrongdoings intended to make personal gains. Moreover, the commitment to ethical values such as fairness, honesty and neutrality requires these agencies to provide reliable information. Competition between these agencies would be another factor that motivates them to exert the best of efforts to provide reliable and fair information calculated on the basis of the going values and costs.

(b) Using the same fundamentals that are followed when appointing and external auditor, in terms of the ownership of shares, the degree of kinship to the members of the board of directors, when appointing estimation and valuation agencies ensures high degree of honesty and objectivity in valuation, since personal bias is absent, and hence that fair value estimations are reliable.

(c) Considering the identification of fair value amongst the management responsibilities, and requiring the management to provide evidences that prove the feasibility of the estimations to the external auditor. This makes

the management seek accuracy in estimations and ensure the reliability of these estimations as a result.

(d) One of the external auditor responsibilities is to collect the evidence related to activities. This includes checking whether the values were recorded properly (according to the standards), that the balances of assets and liabilities appear in the financial statements in proper values, and that the settlements related the assets and liabilities were recorded properly (Al-Thenaibat, 2012). All of that would ensure that information based on fair value recorded in the financial data is reliable to large extent.

Shifting to the components of reliability property the researcher presents the following:

(1) Faithfulness in Representation. It is doubtful that the values based on the historical cost do not truly reflect reality but in one occasion which is the time for purchase or creation. Nevertheless, in the next periods, these values would not reflect reality at all. Hence, fair value should be used since it reflects the reality at the time of financial statements construction.

(2) Neutrality. As mention earlier, the regulation of estimation and valuation agencies ensure the neutrality of these agencies. Hence, the valuation process would be better, and would not be prepared to intentionally serve specific parties.

(3) Verifiability. This can be done by employing a different party to evaluate the same item, had any doubt loomed around the estimations of the first party involved. This would attain, as the research sees, objectivity of the valuation. It is important also to hold the party causing the problem responsible for any extra cost involved.

The above discussions of reliability property components support the research's view in the beginning of the analysis of this feature. Hence they assign a positive answer to the second sub question: the fair value accounting does reinforce the reliability of accounting information.

After discussing and analyzing the two sub questions of the study, the researcher turns to the primary question of the study: Does the application of fair value accounting enhance the quality of accounting information?

Since it attains the two main characteristics of accounting information quality and their elements, the reliance on fair value accounting leads to accounting information with higher quality.

Hence, the answer on the primary question is positive:

The application of fair value accounting does enhance the quality of accounting information.

9. CONCLUSIONS AND RECOMMENDATIONS

9.1. Conclusions

(a) The historical cost principle suffers from several shortcomings. Thus, relying on it in the preparation of financial statements would produce information that does no fulfil the needs of the users of these statements.

(b) The reliance on fair value accounting increases the quality of accounting information, and hence more useful for the users of financial statements.

(c) The reliance on fair value accounting increases the relevance of accounting information, and hence more useful for the users of financial statements.

(d) The reliance on fair value accounting increases the reliability of accounting information, and hence more useful for the users of financial statements.

9.2. Recommendations

Basing on the conclusion drawn, the researcher recommends:

(a) Modifying the theoretical framework of accounting theory to accommodate the application of fair value accounting.

(b) Passing new regulations and legislations which support the use of fair value accounting.

(c) Continuing the transformation toward fair value accounting by the international, regional, and local governing bodies.

(d) Constructing local, regional, and international databases which help in producing fair values for different items.

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