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Positive and Negative Sides of Profit Management

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Abstract: With growing of commercial and business affairs in the world today and getting special of firms directing, the management was isolated from ownership and was charged to professional managers and smart & aware managers to the complex economical and financial problems. Owners have taken their properties to the managers for management accounting due to presenting information and responding against their performance. In this regard, accounting information has provided the huge part of the informational needs of the decision makers. The most accounting information is reflected in basic financial items and more or less the informational need of decision makers such as capital owners, potential investors, credit makers, financial analysts and those other users is done by financial items. Business unit managers are trying to change financial course profit according to providing their policies and goals in different reasons by applying various accounting methods. In present study it has mentioned that the profit equalizing, profit management method, lead to diffuse profit reporting and regarding to the demand increasing for company's stock leads to increasing stock price.

Key words: Profit management · Profit · Profit sides · Positive and Negative sides

INTRODUCTION

According to accepted accounting standards cause of a coherent profit theory, there has been also contradiction between theory makers and professionals in the field of profit reporting and is faced profit reporting with challenges, besides regarding to ownership separation from management the benefits conflict and exclusive availability to some financial information and also promissory accounting particularity in the right of management selecting from different accounting methods there is a possibility to misleading. Besides reported profits are expressed as a financial decision scales. Profit management can be done in managers operational decisions and also shouldn't affect from promissory items. In this research it will studied the different sides of profit management and it concluded about the effect of that on the value of company.

Introducing The Problem and Its Importance: Accounting profit that is accounted and defined based on promissory numbers is a tool for evaluating of company performance. From the other hand the promissory numbers are important indicators for distinguishing the profit quality. Profit quality is also one of the important evaluations of stock because the investors that are the most important group of users of financial items seek their benefit in full quality profit [1].

In general, profit management is possible from two ways: profit management according to accounting numbers and real profit management. In the first type, the management is formed from elective promissory numbers correspond to its favorite goals. But in the second type, the management with taking some operational decisions in other words changing real activities and reaches their real profit, but real profit management leads that operational performance of the company decrease in long period and the company face with irreparable damages [2]. According to some researches, managers in active companies that increase the invest, more goes to profit management and this lead to the decreasing of the feature performance of the company [3-6]. Invest increasing is one of the company's strategies for providing financial resources and the directors are forced to show the firms status better just for creating eager to the investors. Based on Roychowdhury's researches, managers can

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\embellish the profit by applying various methods; some of the applying tools about profit management do no effect on cash currents directly in which include embellishing elective promissory items [7]. Also managers with a motivation of reaching marginal ideal profit or keeping the last year conditions tried to embellish the real financial events that led to the change on cash currents and even on promissory items in some cases. Roychowdhury identifies embellishing in sale such as management attempts according to increasing temporal sale along the year in which is done with presenting discount or easier credit conditions and decrease cash input currents. Therefore it is expected that embellishing in sale led to less cash operational currents in current period. Another type of embellishing is to decrease elective costs. If managers decrease elective costs for increasing profit to mentioned goals, it is expected low elective costs. Third type of embellishing is for preparing expected needs. Additional production decrease prime cost (COGS) which lead to higher operational marginal.

Based on accomplished researches by Gunny and Zang, the tools and strategies of real financial events include speed and acceleration on doing sale, changing goods sending programs, decreasing research and development costs, delay on identifying keeping cost and cash sale discount and decreasing advertisements costs, general costs, administrative and sale, relearning costs and transportation [8, 9].

The studies related to profit embellishing show that the most important factors in this field are reward hypothesis designs, political costs and ownership structure. These hypotheses were tested from 1980 to 1990 [10]. Moses (1987) believes that managers' motivation will be more if the size of the company would be bigger. In his idea bigger in amount of size lead to more responsibility of managers in respond. The numbers of stock in current is not the only indicator for measuring the political sensitivity; the numbers of employees also are another indicator because the more employees so the pressure to the company to reach the goals would be more and finally the management may act along decreasing pressure try to embellish [11].

Due to compensation of creation and innovation, the management mostly gives reward to the managers in finding and implying better work methods. This will lead to create motivation. The company will incur los when managers embellish the profit because when the managers do this act along their goals, the concluded agreements force the company to give more financial rewards. In this way, the embellishing of real activities simultaneously can decrease the performance also enforce more financial agreements to the company [12].

Based on researches, the kind of ownership affects on motivation to the way that if the company belong to the small stockholders that have the short term viewpoint for 4 investment compare with long term investment, so there would be stronger motivation. The inborn ownership is the time that the public organizations have the ownership like financial firms and investment companies. This kind of ownership has a great worth information about the commercial guideline of the company that is taken from direct relationship with management. According to the said information, this the present research tries to answer to this question that how profit management effect on company's value.

The Importance of Financial Information and Managers Actions: For the situation and importance of profit for financial items users, the managers don't pay attention to the way produce and reflect a contrast reaction against the other users of profit. The investors like receive the unfailing information for using to measure them. Managers want to use investment risks. They prefer to cross out their borrowings from balance sheet because they can increase their investments by concluding simple agreements and increase them with loan makers [13]. Also managers prefer to not to clear their accounting methods. This is because of that they can embellish the reported profit by changing their accounting methods in urgent situations. But the investors are aware of the possibility of doing this action by managers, so they concern to this part when they make decision. This theory is a proof that managers have conceptual manner that lead to managers' opportunism that is a conformational logo to this claim. This is so clear that the benefits of the management is related to the select f accounting methods that is just for this reason it is useful for stockholders and investors. Originally it may be a conflict in the benefits between managers and investors, which it could be realized by modeling them like a game. In this situation the game theories can help us to understand how managers and investors could face with their economical outcomes of their financial reports. The game theory tries to predict the benefit conflict between logical and intellectual persons. In conclusion the games theory and the management representation theory that is a kind of known game theories, related on accounting. The management in relation to benefit conflict with investors they are always following a tactic with cost with the most efficiency. This technique can reach with the low probability of resistance or explore and goes to their goals.

The Concept of Profit Management: Profit management in accounting literature can be concerned in the regard of new subjects for managers and is of the issues that introduce in accounting profit. This issue in accounting was formed from the early of 20^{th} century with various researches by theory makers in accounting. Every one of this researches concern in especial dimensions. In accounting literature there were presented different definitions about profit management which will be mentioned later: Healy and Wahlen [14] (1999) believe that profit management occurs when the managers use their personal judges in financial reports and embellish the conclusion structures. This goal is for ignoring of some profit owners or for company economic performance or an effect on the final results of agreements that the personal benefit is on them [14]. Zimmerman and Watts (1990) believe that profit management means applying freedom action on accounting numbers with this hypothesis that there or there is nit any limitation in this field [10]. Schipper (1999) says that profit management is an act from manager that it's doing lead to weakening benefits about information in making decision correspond on standards goals [15].

According to Davidson *et al*. (1998) profit management means the procedure of doing in framework of those principles that accepted in accounting and capable the managers to modify the reported profit to the desirable profit [16].

Sweeny & Sloan believe that profit management means the purposeful interference of management on outgoing organization financial reporting procedure for gaining personal benefits [17]. Builman define profit management as a try from company's management that tries to increase abnormal deviations of profit [18].

Profit management can evaluate from tow two viewpoints which they are conventional or financial repotting. From the first viewpoint, the profit can be a method for protection of company in low cost method. And from the later one, it may present a method by smoothing of profit. Therefore profit management can be as a tool for transferring of outgoing information. Both of the ends with considerable results and profit management could be good too [13]. It may misallocate by some managers. It may be harmed by them. For example the management may bold some lost claims. In some cases extravagance in profit management will decrease reliability. Management in selecting the accounting method between accepted methods is free. Accountants should know profit management because this understanding from financial information and every other beneficiary leads to report better. In this regard selecting accounting methods divide to some classes. One of them is the accounting methods such as direct line versus descending method for calculating depreciation or income identifying methods. The other class is from commitment items like calculating of storage, guarantee cost, the cost of stock value [19]. When the managers with profit management act to increase current profit so know that the reveres of this items in next periods will decrease the feature profit. In fact if the company has the weak performance so the management can't delay the report of this weak performance.

The History of Profit Management: In recent years many researchers have studied the origin of profit management and attributed it to various authors. The term profit management has newly entered into financial literature. In the past the term income smoothing was used instead. Cushing, Pasher and Malcom has attributed it to Gordon, Horwitz and Mires and regards white and Gordon as the origin of theory of income smoothing entrance into financial literature. Imhoff, Ronan and Sadon show, Eckel and Dharan have attributed the identification of income smoothing to Hepworth. Therefore new authors regard it as a new topic which appeared in accounting papers after Hepworth's paper [20].

If instead of the term income smoothing its concept is regarded none of the new authors have not mentioned the origin of income smoothing correctly. There are references from 19^{th} century have dealt with the features of income smoothing by different methods. By simple analysis of the b term income smoothing and focusing on the concept of income smoothing instead of its term has found that 34 papers and books from 1893 to 1953 have identified and explained income smoothing explicitly and implicitly. Johnson and Meadewarshow, Paition and deviance have explained the applications of the theory of income smoothing. Many years before Gordon, Howitz and mires, miler behavior and effects of income smoothing were tested by miler. Early 20^{th} century the relationship between income smoothing, capital maintains and secret reserve was studied. In the second quarter of this century the study of smoothing by the evaluating methods of item was practiced. After world-war II two accounting principles board of America together with accounting authors have focused on bad accounting Principkes. For example Paition's critique on the use of accrual items and change of depreciation method for smoothing profit Anderson opposition to the application of reserves for contingencies to smooth profit and the ban to use reserves as a means to smooth profit in accounting were proposed by the committee of accounting methods many similar papers have been written on the creation of secret reserves for smoothing profit before 1920.

It seems that the most important reason of neglecting of new authors in identifying older researches about profit smoothing is that perhaps before 1950 it hasn't misapplication from the phrase profit smoothing. It can be used some phrases in accounting literature before 1953 due to decreasing frequencies. Some of these phrases are balance smoothing, that were used by Myers and advantage smoothing. In other words the profit smoothing have shifted to profit management nowadays, in the past there were some other common phrases [21]. In concern with above mentioned it seems that the profit management was known in various periods by accounting and financial researchers continuously and now attract some attentions.

Classification of Profit Management: In accounting literature there has been more research about embellishing the accounts. Brining and Stoloy concerns with them classified the profit management to profit smoothing, accumulation of negative items and other profit management sides.

Profit Smoothing: One of the most common kinds of profit management is profit smoothing that means decreasing the profit frequencies in financial periods and reaches that to an acceptable surface. Profit smoothing is an act that is consciously and with using some special tools. Profit smoothing has gained from interpretations and from standards acceptable accounting principles hector stated that Profit smoothing is an act that leads to misusing of financial reporting. Hap worthy stated in this regard that Profit smoothing is an act that can known as false interpretation of financial information. In other words if Profit smoothing is done, the investors will have correct information about profitability to evaluate the outcome and deviation [22].

In concern with the research done in the accounting literature Profit smoothing was divided to two groups: natural smoothing and intentional smoothing that is done by management. The currency of natural smoothing is the result of profit production procedure. And the profited smoothing is the result of real smoothing or artificial. Although artificial smoothing changes the accounting registrations management due to invariable current [23].

Invariable profit is desirable from the viewpoint of an investor and the outcome is low in this kind of company because of the low risk. Based on research, one of the goals of Profit smoothing could be named as risk company decrease. It can be dividing generally in two parts:

- Operational risk: Direct and indirect loss from unsuitable and faulty of inner procedures of persons and systems.
- Company's financial structure risk: it includes two parts: Risk from balance sheet: includes properties, properties structure and properties and debts management. In this field more refer to the various mixtures of them. In other words is the tendency to the property or not. The rate of fixed properties to current properties, the relation of financial properties to physical properties, the volume of properties are some kinds of evaluating indicators of type of financial risk.

The risk of profitability and income: profitability if financial companies, is an indicator that shows the competition situation and managerial ability of the company clearly.

If the profit deviation is low so the operational risk of the company is low. Now the main focus is on financial reporting on predicting of profit and outcome is as an indicator of business unit performance, smooth profit has a great worth as a remarkable element on judging [24].

Negative Items Accumulation: Negative items accumulation means reporting of negative items such an accumulative form in the period of profit or loss. In other words the transfer of feature costs to the little profit. The managers' motivation in this regard may be for the weakest loss. The managers may select the time of that according to interpretation of accounts in bad situations of the last year. This method can rise in some periods that the organizational pressure includes an organizational manager. The new management team can make decision according its own priorities. The management may report the maximum loss because in this situation it will not lost anything. Therefore it decrease the property's value, first it decrease the expectation of feature profitability and prepare it for feature, second it will be a base for increasing profit and providing company in feature [14].

Other Sides of Profit Management: As said before, managers make profit with different motivations like reward, maintain of debit agreements and also political goals. In this situation the goal of effecting on profit is with the relation goals. For example about keeping and maintaining of debits agreements, the managers are eager to report the profit such a way to maintain the goals. This is for decreasing the cost of political goals and also decreasing profit. About the rewards goals, the manager perhaps wants more profit report or less that real.

CONCLUSIONS

In this research the various sides of management was studied. Despite of shortcomings of profit management, the profit smoothing is a profit management method that leads to decrease the profit along different years and attend the reliability of investors and buying stocks and finally increasing the cost of the stocks.

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