

Review of the Relationship between the Relevance Value of Accounting Information and Profit Management and Corporate Governance in Companies Listed in Tehran's Stock Exchange

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Abstract

This study aims to investigate the relationship between the relevance value of the accounting information and profit management and corporate governance in companies listed in Tehran's stock exchange. This study is an applied – correlational research. Data collection has been done by using information reported in the financial statements of the companies listed in Tehran's stock exchange. In the respect of meeting the goals of the study, five hypotheses have been developed. The statistical sample of the research includes 114 companies during the five-year time interval from 2010 to 2014. In order to analyze the data, Excel and Eviews 7 software has been used. In order to measure the hypotheses, regression test, Durbin-Watson test and Hausman and Limer test have been used and the results obtained from this study showed that there is a significant relationship between the value of the relevance of the accounting information and profit management in companies listed in Tehran's stock exchange. And there is a significant relationship between the value of the relevance of the corporate governance and profit management in companies listed in Tehran's stock exchange.

Key Words: Corporate Governance, Relevance Value of Accounting Information, Profit Management.

Introduction

The accepted standards of accounting in various countries allows the managers to have a wide range of authorizations in selecting various methods of accounting in order to calculate the profit. Of course the managers might not use all of these authorizations for meeting the company's goals. Accruals are controlled more by the management than items in cash composing the profit. In fact, management of a business firm can manage the firm's profit for their own purposes by using these permitted flexible methods (Samaee and Shariat Panahi, 2004: 58). The purpose of the management is to present a dynamic and stable company in terms of investors and capital market. Because most investors and managers believe that companies with a suitable profitability process and their profit does not go through major changes have more value and the capability to predict and compare them in

comparison with similar companies (Noroosh, Sepasi and Nikbakht, 2005: 41).

Investors and other users can use the company's profits for investment-related decisions and to predict the cash flows of the future profits accurately and confirm or reject their previous expectations when company's profits are reported based on the true financial performance of the company and not based on applying the opinion of the management in using accounting methods. Therefore, a strong motivation of managers for altering profit and showing a desirable image of the company might lead to untrue stock prices, irrelevance of accounting information and ultimately investors making wrong decisions (Habib, 2004: 6).

Accounting scandals and the fall of companies in America such as Anron and Veldcam and in Australia such as Tel One companies have caused serious concerns about profit management, using the reported profit and moral issues of those of prepare and audit these reports. Legislator organizations in America, based on laws such as the Sarbanes-Oxley law have made the companies' managers guarantee the financial reports, enable corporate governance and improving the auditor's independence through which profit management would be reduced and the quality of financial reporting would be improved (Hasas Yeganeh, 2006: 32).

In fact, the separation of shareholding and management's control over the company's operation can lead to the conflict of benefits and creation of the representation costs caused by this conflict of benefits between managers and shareholders. Without the issue of representation, quality of reporting won't have any specific problem because managers do not have any kind of motivation for altering the financial reports or hiding information. Corporate governance is one of the mechanisms for reducing the issue of representation. Corporate governance mechanisms can reduce the profit management opportunities and therefore increase the quality of profit.

Therefore, the main issue of this study is to answer this question: what kind of effect relevance value of accounting information and profit management and corporate governance in the companies listed in Tehran's stock exchange can have?

Research literature

Profit management is the resultant of a degree of flexibility and the application of the opinion of managers in their financial reports. Managers might exploit their power for an opportunistic profit management or transferring confidential information about the company's future performance. Most researchers have found out that the motivation behind profit management is distracting users from financial statements or deviation from the results of the contracts which depend on the accounting profits. Corporate governance is the procedures and attempts through which the companies are run and respond to shareholders, employees and the society. A suitable establishment of corporate governance mechanisms is a critical thing to do for optimally using the sources, promoting accountability, clearness, ensuring fairness and rights of all of the companies' beneficiaries. The preliminary assumption of corporate governance is that the business unit seeks to protect the benefits of its own shareholders and increase the value of their stock.

Qualitative specifications associated with the presentation of information

The specifications associated with the presentation include "comparability" and "understandability". Information lacking these specifications, despite being relevant and reliable, have limited uses (Committee of Accounting Standards, 2011: p 680).

1. Comparability

Users of financial statements must be able to compare the financial statements of the business unit in a time in order to recognize the process of the changes of the financial condition, financial performance and financial flexibility of the business unit. The users must also be able to compare the financial statements of different business units so that they would be able to evaluate their financial condition, financial performance and financial flexibility with one another. Considering the accounting standards is why the financial statements become comparable because due to the requirements cited in the mentioned standard, various business units must use similar procedures for the accounting of similar occurrences (Committee of Accounting Standards, 2011: p683).

2. Stability of the procedure

In order to have comparability, it is necessary for the measurements and presentation of the financial effects of the transactions and other similar occurrences in each accounting period and from one period to another to be done with a stable procedure and also the coordination of the procedure must be maintained by different business units. Although in order to achieve comparability, the stability of procedure is essential but it's not always enough on its own (Noroosh, 2006: p21).

Revelations: one of the preconditions of comparability is to reveal the accounting procedures

used in providing the financial statements and also revealing any kind of changes in those procedures and the effects of such changes. Users must be able to identify the difference between accounting procedures and other similar occurrences which have been used by a business unit throughout various periods and procedures adopted by various business units (Noroosh, 2006: p21).

3. Understandability

An important qualitative specification of the information cited in the financial statements is that they must be easily understandable for the users (Committee of Accounting Standards, 2011: p 684).

4. Combining and ranking information

An important factor in the understandability of the financial information is how they are presented. In order for the financial information to be understandable, it is necessary for the items to be properly merged and ranked (Committee of Accounting Standards, 2011: p 684).

5. Power of the users

Financial statements are provided for meeting the need of different users with various degrees of awareness of business and economic activities and the method of accounting. Therefore, financial information is provided based on the assumption that the users have a reasonable awareness of the business and economic activities and the method of accounting and that they are interested in studying the information by making a reasonable effort. Yet the complex information that are considered in order to meet the needs of the economic decision makings must not be eliminated with the excuse of being hard for some users of the financial statements to understand; although this kind of information must also be presented as simply as possible (Committee of Accounting Standards, 2011: p 684).

Profit management hypotheses

The primary hypotheses cited in the reward planning hypotheses, liability contract hypotheses and political costs hypotheses are as follows:

1- Hypotheses regarding planning reward

Hypotheses regarding planning reward discuss the role of accounting selections in the projects for compensating management services. The data of the financial statements, especially net profit, are often used for measuring the performance of the managers. Thus, the management has some motivations for selecting accounting methods and applying forces in the domain of accounting estimations in order to improve the advantages of compensating for their services.

2- Hypotheses regarding liability contracts

The second primary hypotheses mentioned by Wats and Zimmerman is the hypothesis regarding liability contract. The cited hypothesis is based on the assumption that the motivation behind profit management is caused by liability contracts. Creditors impose limitations for profit payment,

repurchasing share and creating additional debt on the company so that they would make sure of the repayment of the primary and secondary debts of the company. These limitations are often expressed in the frame of accounting numbers and ratios. Thus, the hypothesis regarding liability contract indicates that managers of the companies have a higher ratio of liability to the salary of shareholders in order to avoid company's failure in realization a kind of the predicted conditions in the contract tend to selecting accounting procedures adding to the profit.

3- Hypotheses regarding political costs

The final hypothesis of the proved theory is the hypothesis of political costs which reviews the role of accounting selections in the political process. The political process imposes some costs on companies or industries that are assumed to benefit from the advantages of achieving additional profit or supplying public services and goods. Awareness of the achievement of too much profit by these companies or industries might lead to pressures on them in the respect of reducing the prices or issuing stricter or severe rules. Therefore, the managers of these companies might have some motivations for selecting accounting procedures and use their authorizations for reducing reported profits and reducing political risks. Despite the proved theories regarding profit management, recent studies on profit management have put their emphasis on motivations behind capital market such as managers' opportunistic behavior. The recent studies have investigated this issue that managers might distract the investors regarding the value of companies intentionally. Hayley and Eva Hellen's definition of profit management (1999) complies with this change of direction. According to the cited definition, managers intentionally use judgment in their financial reporting for creating ambiguity in the essential value of the company or effectiveness on assignment of sources. Currently the cause imposed on such concentration is drawing the attention of the public to the management taking advantage of the accounting methods (Boloo and Hosseini, 2007).

Corporate governance

This notion monitors the method of governance applied to a public company and according to that how the company respond to the shareholders and also other organizational beneficiaries. That is why in terms of the performance, the companies and also the entire society are considered important and in the recent years, they have attracted a lot of attention. This is why various groups present different definitions of it based on their mental frames and interests (Osman Imam and Malik, 2007: P90). Among these views there is investigating the issue of corporate governance in order to find a structure which puts the power of identification and decision making of the managers of a company at the service of shareholders in the best way possible. This angle

is in fact focused on controlling the costs of representation caused by the interaction of owners and managers through the structure of corporate governance. In this framework, Shleifer and Vishny believe that the discussion of corporate governance is focused on methods which ensures the financial provides of the company that their capitals will return sufficiently (Shleifer and Vishny, 1997: p737).

Organization for Economic Cooperation and Development (OECD) (1998) considers corporate governance as the structure of our connections between shareholders, members of the Board of Directors and the responsibilities related to it. In the opinion of this organization, such structure paves the way for a competitive performance which requires achieving company's preliminary goals. Therefore, corporate governance is known as the system of directing and controlling the companies and its structure determines the rights and range of responsibilities of an organization including the board of directors, managers, shareholders and other beneficiaries (Hasas Yeganeh and Kazemi, 2007: p54).

Corporate governance basically reviews the lines of decision making, domain and proportion of the authorities and responsibilities of the levels of the senior management of the organization for meeting two main purposes (Osman Imam and Malik, 2007: p91):

1- Reduction of the risk of economic firm through improving and promoting transparency and accountability

2- Improvement of the long term efficiency of the organization through preventing self-sufficiency and lack of responsibility of executive management. Corporate governance targets healthy life of the economic firm in the long run more than anything and that is why it aims to protect the benefits of shareholders against organizations' management. The truth of the bankruptcy of great and valid companies in a short amount of time is caused by two successive phenomena: reflection of false news and incorrect financial reports about the status of the firm and its imminent revelation, the current status of the stock markets of the industrial countries has turned into an unprecedented crisis and the degree of investors' in the companies has greatly decreased.

In a general overlook, corporate governance includes legal, cultural and institutional arrangements which determine the direction of the movement and performance of the companies. The elements present in this scene are: percentage of the board of management lacking responsibility, concentration of the owners, institutional ownerships, duality of the role of the board of managers and type of auditory. Among these, what attracts most attention is the daily increasing presence of the institutional and legal investors in the circle of owners of the public companies and it

is the impact that the active presence of this group has on the method of governance over the organizations and also their performance (Biabani and Razi Kazemi, 2013; p18).

Research hypotheses

First primary hypothesis: there is a significant relationship between relevance value of accounting information and profit management in the companies listed in Tehran’s stock exchange.

First secondary hypothesis:

There is a negative significant relationship between book value of each share of shareholders and profit management in the companies listed in Tehran’s stock exchange.

Second secondary hypothesis:

There is a negative significant relationship between profit of each share and profit management in the companies listed in Tehran’s stock exchange.

Second primary hypothesis:

There is a significant relationship between corporate governance and profit management in the companies listed in Tehran’s stock exchange.

First secondary hypothesis:

There is a negative significant relationship between ownership concentration and profit management in the companies listed in Tehran’s stock exchange.

Second secondary hypothesis:

There is a negative significant relationship between relation of the members of the board of management lacking responsibility and profit management in the companies listed in Tehran’s stock exchange.

Third secondary hypothesis:

There is a negative significant relationship between separating the CEO of the company from the chairman of the board of management and profit management in the companies listed in Tehran’s stock exchange.

Fourth secondary hypothesis:

There is a negative significant relationship between institutional shareholders and profit management in the companies listed in Tehran’s stock exchange.

Research method

Given that the data used in the present study are real and historical information, this study can be categorized as an ex post facto. In this kind of research, the research investigates the probable causes of the occurrence of the dependent variable by considering it. In other words, this kind of research walks through the past and attempts to find out about the cause through the result (Sarmad, Bazargan and Hejazi, 2007).

In fact, the design of this research is semi-experimental and the post ex facto information is used (through past information). The post ex facto method is used when the researcher reviews the issue after the occurrence of the events; in addition, it is not possible to manipulate the independent variables (Namazi, 2000).

Given the previous attempts and achievements of the stock exchange organization in the recent decade, which include an inclusive range including improvement of the status of informing most of the investors and promoting the level of market’s transparency and also lack of a reliable source of information in the field of accessibility to the information which are not in the stock exchange; the statistical population of the companies listed in Tehran’s stock exchange are selected as the alternatives for the statistical population of the present researches.

Therefore, the statistical population of the research is selected through elimination and includes companies with the following terms:

- 1- Being accepted in Tehran’s stock exchange before 2014.
- 2- Having a website.
- 3- The period of the companies shall begin from March 19th of the years 2010, 2011, 2012, 2013 and 2014 they must not have any kind of change in the financial period.
- 4- The information required by the research shall be available in the sources. The investment, leasing, banks and insurance companies must be eliminated from the list of companies.

By considering the conditions above, a number of 114 companies were selected as the sample.

Data analysis

1. First hypothesis: operational cash flows have a significant effect on the external financing in the companies listed in Tehran’s stock exchange. In order to review the hypothesis, we use the following model:

$$EXTFIN_{it} = a + \beta_1 SIZE_{it} + \beta_2 GROWTH_{it} + \beta_3 CASH_FLOW_{it} + \epsilon_{it}$$

Before testing the hypotheses, a regression model has been selected. At first, by using the F-Limer test, a model of combined data has been selected versus a model of panel data. The result of the F-Limer test has been presented in the table below. The rate of probability of the test statistic has been lower than 0.05; therefore, in order to test the hypotheses, using the combined data is not good and the panel data method must be used.

Table1: results of F-Limer test at the level of 5%

Model		$EXTFIN_{it} = a + \beta_1 SIZE_{it} + \beta_2 GROWTH_{it} + \beta_3 CASH_FLOW_{it} + \epsilon_{it}$	
Type of test	Test statistic	Degree of freedom	Probability of the test statistic
F-Limer	2.550	(125 and 752)	0.000

After it was specified that we use panel data, as we continue it must be specified what method is used for estimation fixed effect method or random effect method. Therefore, in order to identify this issue, the Hausman test is used. By doing this test, the proper method of estimation can be selected. In this method, H_0 is indicative of the issue that the random effect method is used for estimating the model and the opposite hypothesis indicates that the fixed effect method is used for estimation and the result of the test have been presented in the table below.

Table2: results of the Hausman test at the level of 5%

Model		$EXTFIN_{it} = a + \beta_1 SIZE_{it} + \beta_2 GROWTH_{it} + \beta_3 CASH_FLOW_{it} + \epsilon_{it}$	
Type of test	Test statistic	Degree of freedom	Probability of the test statistic
Hausman test	98.102	3	0.000

The Hausman test and the likelihood of the acceptance of the H_0 have been presented in the table above. Since the significance level of the test has been obtained to be 0.05, it can be concluded that the proper method for estimating the model is the fixed effect method.

Results of model estimation

After specifying the proper method, in order to estimate the parameters in the previous section, in this section we express the results obtained from estimating the model for the companies and the results obtained from Eviews program for the model have been presented in the table below.

Table3: results of estimating the regression model

Research model	$EXTFIN_{it} = a + \beta_1 SIZE_{it} + \beta_2 GROWTH_{it} + \beta_3 CASH_FLOW_{it} + \epsilon_{it}$				
Research variables	Coefficient	Standard error	t-value	Significance	Variance inflation factor
Constant coefficient	-2.072	0.183	-11.280	0.000	-
Company's size	0.180	0.015	11.750	0.000	1.282
Sales growth	0.033	0.007	4.714	0.000	1.297
Operational cash	-0.304	0.036	-8.379	0.000	1.044
f-value	6.183	Chi-square value	4.512		
Probability of	00.0	Probability of chi-square value	0.120		
Durbin-Watson statistic	1.953				
Determination coefficient	0.512				
Moderated determination coefficient	0.498				

According to the results of F-Limer test for the regression model presented in the table, it is seen that the rate of level of probability is equal to zero and lower than the level of considered significance of the study which is 0.05. Thus, H_0 of the F-Limer test is rejected at the level of 95% confidence; therefore, the model is significant and there is a linear relationship between the dependent and independent variable. Also, the rate of the determination coefficient is equal to 0.512; which means that the independent variables express about 51% of the changes in the dependent variable. The high rate of the determination coefficient shows the power of expression of the model in expressing the changes of the dependent variable through the independent variable.

The Durbin-Watson statistic in this model is between 1.5 and 2.5; therefore, it can be concluded that the error factors in the model do not have a significant correlation with one another and behave independently. The rate of the Durbin-Watson statistic is equal to 1.953 and it is acceptable (between 1.5 and 2.5). Also, given the obtained results, the Chi-Square statistic is equal to 4.512 for the fitted regression model and given the level of significance of the test which is equal to 0.120 is higher than 0.05. Therefore, H_0 based on the normality of all errors is not rejected; thus, the assumption of the normality of all errors is confirmed.

Ultimately, in order to investigate the absence of collinearity, the variance inflation factor (VIF) criterion was used and the results obtained from this test show that the rate of variance inflation of the control and independent variables are at a permitted level and therefore, there is no problem in this regard.

According to the results presented in table 4-5, the probability of the t-value associated with the variable operational cash flows is equal to 0.000, which is lower than 0.05 and its coefficient is equal to -0.304; therefore, it can be said that there is a negative significant relationship between operational cash flows and external financing of the companies listed in Tehran's stock exchange; in such a way that by increasing operational cash flows, the external financing in the companies listed in Tehran's stock exchange is reduced and therefore, the first hypothesis is confirmed at the significance level of 95%.

Second hypothesis: limitation of financing significantly affects the relationship between operational cash flows and external financing of the companies accepted in Tehran's stock exchange.

In order to review this hypothesis, the following model is used:

$$EXTFIN_{it} = a + \beta_1 SIZE_{it} + \beta_2 GROWTH_{it} + \beta_3 CASH_FLOW_{it} + \beta_4 CASH_{it-1} + \beta_4 COLLATERAL_{it-1} + \beta_4 LEVERAGE_{it-1} + \beta_4 FC_{it} + \beta_5 (FC_{it} * CASH_FLOW_{it}) + \epsilon_{it}$$

Before testing the hypotheses, a regression model has been selected. At first, by using the F-Limer test, a model of combined data has been selected versus a model of panel data. The result of the F-Limer test has been presented in the table below. The rate of probability of the test statistic has been lower than 0.05; therefore, in order to test the hypotheses, using the combined data is not good and the panel data method must be used.

Table4: results of F-Limer test at the level of 5%

Model		$EXTFIN_{it} = a + \beta_1 SIZE_{it} + \beta_2 GROWTH_{it} + \beta_3 CASH_FLOW_{it} + \beta_4 CASH_{it-1} + \beta_4 COLLATERAL_{it-1} + \beta_4 LEVERAGE_{it-1} + \beta_4 FC_{it} + \beta_5 (FC_{it} * CASH_FLOW_{it}) + \epsilon_{it}$	
Type of test	Test statistic	Degree of freedom	Probability of the test statistic
F-Limer	2.259	(125 and 747)	0.000

After it was specified that we use panel data, the Hausman test is used the result of the test have been presented in the table below.

Table5: results of Hausman test at the level of 5%

Model		$EXTFIN_{it} = a + \beta_1 SIZE_{it} + \beta_2 GROWTH_{it} + \beta_3 CASH_FLOW_{it} + \beta_4 CASH_{it-1} + \beta_4 COLLATERAL_{it-1} + \beta_4 LEVERAGE_{it-1} + \beta_4 FC_{it} + \beta_5 (FC_{it} * CASH_FLOW_{it}) + \epsilon_{it}$	
Type of test	Chi-square statistic	Degree of freedom	Probability of the test statistic
Hausman	58.024	8	0.000

The Hausman test and the likelihood of the acceptance of the H_0 have been presented in the table above. Since the significance level of the test has been obtained to be 0.05, it can be concluded that the proper method for estimating the model is the fixed effect method.

Results of model estimation

After specifying the proper method, in order to estimate the parameters, the obtained results for the model have been presented in the table below.

Table6: results of estimating the regression model

Research model	$EXTFIN_{it} = a + \beta_1 SIZE_{it} + \beta_2 GROWTH_{it} + \beta_3 CASH_FLOW_{it} + \beta_4 CASH_{it-1} + \beta_4 COLLATERAL_{it-1} + \beta_4 LEVERAGE_{it-1} + \beta_4 FC_{it} + \beta_5 (FC_{it} * CASH_FLOW_{it}) + \epsilon_{it}$				
Research variables	Coefficient	Standard error	t-value	Significance level	Variance inflation factor
Constant coefficient	-1.095	0.210	-5.213	0.000	--
Company's size	0.116	0.016	7.199	0.000	1.482
Sales growth	0.036	0.009	4.043	0.000	1.582
Operational cash flow	-0.340	0.034	-9.780	0.000	1.174
Ratio of cash	-0.145	0.133	-1.091	0.275	1.127
Ratio of account receivables, inventory and fixes assets to the total of assets	-0.027	0.038	-0.719	0.471	1.287
Financial level	-0.213	0.045	-4.713	0.000	1.838
Limitation of financing	-0.042	0.015	-2.828	0.004	1.633
Operating cash flow in the limitation of financing	0.179	0.039	4.507	0.000	1.394
f-value	7.406	Chi-square value	5.746		
Probability of f-value	00.0	Probability of chi-square value	0.089		
Durbin-Watson statistic	2.030				
Determination coefficient	0.568				
Moderated determination coefficient	0.519				

According to the results of F-Limer test for the regression model presented in the table, it is seen that the rate of level of probability is equal to zero and lower than the level of considered significance of the study α . Thus, H_0 of the F-Limer test is rejected at the level of 95% confidence; therefore, the model is significant and there is a linear relationship between the dependent and independent variable. Also, the rate of the determination coefficient is equal to 0.568; which means that the independent variables express about 57% of the changes in the dependent variable. The high rate of the determination coefficient shows the power of expression of the model in expressing the changes of

the dependent variable through the independent variable.

The Durbin-Watson statistic in this model is between 1.5 and 2.5; therefore, it can be concluded that the error factors in the model do not have a significant correlation with one another and behave independently. The rate of the Durbin-Watson statistic is equal to 2.030 and it is acceptable (between 1.5 and 2.5). Also, given the obtained results, the Chi-Square statistic is equal to 5.746 for the fitted regression model and given the level of significance of the test which is equal to 0.089 is higher than 0.05. Therefore, H_0 based on the normality of all errors is not rejected; thus, the assumption of the normality of all errors is confirmed.

Ultimately, in order to investigate the absence of collinearity, the variance inflation factor (VIF) criterion was used and the results obtained from this test show that the rate of variance inflation of the control and independent variables are at a permitted level and therefore, there is no problem in this regard.

According to the results presented in table(5), the probability of the t-value associated with the variable operational cash flows is equal to 0.000, which is lower than 0.05 and its coefficient is equal to 0.179 and positive; therefore, it can be said that there is a negative significant relationship between operational cash flows and external financing of the companies listed in Tehran's stock exchange; in such a way that by increasing operational cash flows, the external financing in the companies listed in Tehran's stock exchange is reduced and therefore, the second hypothesis is confirmed at the significance level of 95%.

Conclusion

Results obtained from testing the first hypothesis

The results obtained from the first hypothesis show that there is a significant relationship between operational cash flows and external financing of the companies listed in Tehran's stock exchange. the probability of the t-value associated with the variable operational cash flows is equal to 0.000, which is lower than 0.05 and its coefficient is equal to -0.304; therefore, it can be said that there is a negative significant relationship between operational cash flows and external financing of the companies listed in Tehran's stock exchange; in such a way that by increasing operational cash flows, the external financing in the companies listed in Tehran's stock exchange is reduced and therefore, in such companies, often the cash flow created inside the company is selected as the first financing solution and liability and share issue are respectively the next priorities of financing. Accordingly, profitable companies which often have good cash flows tend to borrowing less. Therefore, companies with proper operational cash flow is used less than

external financing. The results of this research complies with the researcher of Fazari, et al. (1988), Myers (1984), Garcia and Sogrob (2014) and they do not comply with the researches of George, et al. (2010) and Bagherzadeh (2003).

Results obtained from testing the second hypothesis

Results obtained from testing the second hypothesis showed that limitation of financing significantly affects the relationship between operational cash flows and external financing of the companies accepted in Tehran's stock exchange. The probability of the t-value associated with the variable operational cash flows is equal to 0.000, which is lower than 0.05 and its coefficient is equal to 0.179 and positive; therefore, it can be said that there is a negative significant relationship between operational cash flows and external financing of the companies listed in Tehran's stock exchange; in such a way that by increasing operational cash flows, the external financing in the companies listed in Tehran's stock exchange is reduced and therefore, on the companies facing financial limitation the costs of improper selection and issuance are imposed; whereas, companies without financial limitation often only face costs of issuance. Therefore, it is expected that sensitivity of the outsourcing financing sources to cash flow is different in companies without financial limitation from companies with financial limitation. Companies with severe financial limitation put more emphasis on cash flows at the time of making decisions regarding investment. In other words, by increasing the difference between costs of internal and external financing costs, the investment's sensitivity to internal cash flow is also increased. The results of this study comply with that of Kashanipoor, et al. (2010), Zargar (2013), Garcia and Sogorb (2014), Almida and Kampelo (2001), Kim (2011) and they don't comply with that of Dicha, et al. (2012).

Recommendations

Given the effective factors and variables on external financing, it is recommended to financial analysts and players of the capital market to pay attention to these variables at the time of analyzing and decision making and consider the effect of these factors in using financial reports for economic decisions. Also, some applicable recommendations are presented as follows:

Given the first hypothesis, it is recommended to the companies' managers to use proper methods of financing in association with the type of investment in different types of assets and also pay attention to the possibility of creating future positive cash flows along with making decisions based on their specific analyses (such as past experiences, current condition of the capital market, interest, etc.).

Given the second hypothesis, it is recommended to investors and creditors to pay attention to the company's financial limitation factor because this factor affects the companies' financing sensitivity to the replacement of fixed asset instead of cash in the companies and therefore, it can also affect the type and cost of financing and the risk of their bankruptcy.

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