Al-imad Journal of Humanities and Applied Sciences (AJHAS)
مجلة العماد للعلوم الإنسانية والتطبيقية
ISSN: 3106-0323
Volume 2 – Issue 1 – 2026
Pages 1159-1164

Financial Reporting and Its Impact on Decision-Making

Muftah Faraj* [1], Jumia O. A. Madi [2], Abdulsalam M. A. Altarhouni [3]
[1,2,3] Department of Administrative and Financial Sciences, Faculty of Technical Sciences, Sebha, Libya
*Corresponding: jumiamadi@yahoo.com

التقارير المالية وأثرها على اتخاذ القرار

مفتاح فرج عبدالجليل فرج [1]، جمعه عثمان على مادي * [2]، عبدالسلام محمد احمد الترهوني [3]
[3،2،1] قسم العلوم الإدارية والمالية، كلية العلوم التقنية سبها، سبها، ليبيا

Received: 01-05-2026; Accepted: 04-06-2026; Published: 17-06-2026

Abstract
Financial reports have become a vital tool in the financial decision-making process, encompassing planning, organizing, directing, and controlling. Their application is not restricted to a specific individual or a particular managerial level; rather, everyone is required to utilize them to discharge their duties and facilitate decision-making effectively. In doing so, the decision-maker seeks the most acceptable alternative within the limits of the information available to them; thus, the success of any organization. Financial decision-making hinges upon the content of financial reports, which are characterized by a specific set of attributes. This is due to their critical role in guiding decision-makers—enabling them to identify the most appropriate solutions to problems and assess the extent of their impact on achieving desired objectives. Indeed, financial decisions are inextricably linked to Financial reports ; a sound decision is fundamentally grounded in financial reports that adhere to specific standards and defined characteristics, thereby assisting the decision-maker within an organization in realizing their goals.

Keywords : Financial Reporting, Decision-making, Financial Statements, Ratio Analysis, IFRS, Shareholder Wealth, Business Quality.

الملخص
أصبحت التقارير المالية أداة مهمة وحيوية في عملية اتخاذ القرارات المالية، بحيث تشتمل على جوانب التخطيط، والتنظيم، والتوجيه، والرقابة. ولا يقتصر استخدام هذه التقارير على فرد بعينه أو مستوى إداري محدد؛ بل يُعد توظيفها أمراً مطلوباً من الجميع لأداء واجباتهم وتسهيل عملية اتخاذ القرارات بفاعلية. وفي سياق ذلك، يسعى صانع القرار إلى اختيار البديل الأكثر قبولاً في ضوء المعلومات المتاحة لديه؛ وهو الأمر الذي يمثل ركيزة أساسية لنجاح أي مؤسسة. ان اتخاذ القرارات المالية بشكل جوهري ترتكز على محتوى التقارير المالية، التي تتميز بمجموعة محددة من الخصائص والسمات. ويعود ذلك إلى الدور البالغ الأهمية الذي تؤديه هذه التقارير في توجيه صانعي القرارات، وتمكينهم من تحديد الحلول الأنسب للمشكلات، وتقييم مدى تأثير تلك الحلول في تحقيق الأهداف المنشودة. والواقع أن القرارات المالية ترتبط ارتباطاً وثيقاً لا انفصام فيه بالتقارير المالية؛ إذ إن القرار السليم يستند في جوهره إلى تقارير مالية تلتزم بمعايير محددة وخصائص واضحة المعالم، مما يعين صانع القرار داخل المؤسسة على بلوغ غاياته وتحقيق أهدافه.

الكلمات المفتاحية: التقارير المالية، اتخاذ القرار، القوائم المالية، تحليل النسب، المعايير الدولية للتقارير المالية (*IFRS*)، ثروة المساهمين، جودة الأعمال.

Introduction

Today, managers are sometimes required to make decisions in a volatile business environment. These decisions might include process decisions to reduce a number of overheads to increase profits. However, only managers who have a proper understanding of the company's financial statements can be able to make sound investment decisions. Thus, it is essential for the manager to be familiar with financial statements to make informed decisions. There are different types of financial statements that can be used to obtain information for decisions making. These financial statements include a statement of financial performance, statement of financial position, and cash flow statement (Li, 2016). Managers can obtain information directly from the financial statement or use other methodologies to make decisions. For instance, Li (2016) points out that managers can compute ratios from the balance sheet to establish whether a company is financially healthy. Ratio analysis is one of the best techniques used by both managers and investors to obtain specific information from financial statements for decision-making. The main objective of accountants is to ensure they prepare financial statements in a standardized format that can be utilized for decision-making. According to Li (2016), ratio analysis is used to make decisions because financial statements follow a standardized structure that is not relevant to users. Moreover, Van Auken and Yang (2014) assert that statements are only a record of financial information with evaluation of the data. Therefore, different users of financial statements must have the capacity to "read" the content of the statements to make sound decisions.

Aims and objective of the study

The main objective of this study is to establish how financial information helps managers in decision-making. Specifically, it identifies the role of financial reporting in investment decisions. The financial statements must be able to provide a realistic objective of the business condition so that managers can make decisions. Thus, auditing of financial statement is critical to ensure financial statement represent the fair view of the financial position of the firm. This study also discusses how financial statements are prepared and the different ways they can be used to make decisions.

Research Objective

The aims of this study will be achieved by discussing how financial statements are prepared. Secondly, the study will identify methods that can be used by both managers and investors to analyze financial statements to make a rational decision. The most commonly used method to analyze raw data presented in financial statements is ratio analysis (Van Auken & Yang, 2014). Analyzing financial information involves the rearranging of information in a manner that allows users to appraise the performance, financial health, and growth potential of the company. To be able to attain an effective evaluation of financial statements, it is essential to conduct a superficial analysis of the statements to determine the area that requires attention. For instance, it is critical to start with an evaluation of the statement of funds to establish the ability of the company to generate cash. This will be followed by ratio analysis to determine the financial risk, profitability, and management efficiency in utilizing assets to generate profits.

Financial Reporting Standards

There is the need to set financial reporting standards because they enhance high-quality accounting and auditing in enterprises. The agencies are supported by robust regulations, ethical and governance framework (Timm, 2016). Therefore, proper financial reporting standards are imperative in organizations.

The International Finance Reporting Standards (IFRS) began when the Standing Interpretation Committee Standards (SICS) principles merged with International Accounting Standards (IAS) in April 2001 (Timm, 2016). The IFRS standards developed as an attempt to complement accounting across the countries within the European Union. Conversely, the concept became attractive across the corporate world. IFRS has provided a common business language in accounting and finance, which is understandable by all companies in the globe.

The collaboration between International Integrated Reporting Council (IIRC) and IFRS highlights the common interest. They improve the quality and consistency of the global corporative reporting in business institutions. The organizations promote clarity in commercial reporting framework in a way that drives comparability and coherence (Eng, 2014). The values improve the effectiveness and efficiency of corporate reporting practices. Additionally, the collaboration has ensured transparency and sharing of significant information between corporates.

The pivotal development of the financial reporting is the creation of a system that adopts the conceptual approach in developing the corporative accounting standards. The financial reporting has created a harmonized and shared business language in account reporting all over the globe (Rahimi, 2016).

The International Accounting Standards Board (IASB) has had a significant impact on the financial reporting in the past five years. The agency has promoted transparency and easy comparison in transactions within corporates (Akgün, 2016). Companies can enjoy transparent and efficient financial accounting within their jurisdiction or across the borders.

Decision Making using Financial Statements

For managers and investors to make good use of financial information, it is important for them to analyze financial statements. Financial analysis can be denoted as the process by which financial data is converted into useful information for decision-making, achieved by different analytical methods such as ratio analysis which is essential in establishing lucid pronouncements (Van Auken & Yang, 2014). Thus, it is vital for managers to know the current position of the business. Financial analysis always comes before decision-making and planning of management process. Therefore, the financial analysis highlights the importance of users to have a general knowledge of financial analysis to make informed decisions. Proper financial planning has to take into account all the strength and weakness of the company. Financial analysis, according to Van Auken and Yang (2014), identifies good characteristics of the company so that they can be used to pin-point the weakness of the company to take corrective actions. Thus, it is reasonable to conclude that managers are the most significant users of financial statements.

During financial analysis, managers can utilize a range of instruments and techniques. There are different methods that can be used to achieve these goals, for instance, by using horizontal and structural financial statements, and vertical analysis. As explicated by Li (2016), a horizontal analysis is based on comparative financial statements which tries to establish the dynamics of changes of financial statements. The efficiency of the company is established by observing the basis of changes in financial statements. A structured financial statement is used as a basis for vertical analysis because it analyses the structure of financial statements (Li, 2016). The business structure is critical to a business because it establishes business quality. Although both vertical and horizontal analysis are used to analyze financial statements, Van Auken and Yang (2014) argues that they do not identify business quality. However, ratio analysis can be used to analyze financial statements for decision-making.

Literature Review

There is a wide range of literature that talks about theories of financial statements, including residual equity theory, social theory, enterprise theory and proprietary theory, all elucidated by Van Auken and Yang (2014). According to proprietary theory, accountants should prepare financial statements from the shareholders perspective. On the other side, residual theory, coined in by Staubus in 1952, argues that accounting information should be prepared from the residual equity holder's perspective. The residual theory's argument is consistent with the going concern which requires financial statements to be prepared from common shareholders perspectives. However, the residual theory has been regarded to be more restrictive of proprietary theory. According to the proprietary theory, financial reporting record transaction and events for their immediate impact on the proprietor. It argues that financial statements are prepared from the proprietor's perspective which can be expressed by the following accounting equation:

$$\text{Net worth/Equity} = \text{Total asset- Total liability}$$

When using the proprietary viewpoint, the total assets in the statement of financial position are considered the assets of the proprietor and the liabilities are the proprietor's liabilities. According to proprietary theory, financial liabilities represent negative assets of the proprietor while revenues represent an increase in the assets of the proprietor. The revenues are represented by the surplus of revenues over expenses accrues to the proprietor. This revenue represents an increase in shareholders wealth. Staubus also studied the role of preferential shareholders in the proprietor's financial statements. He highlighted that preferential shareholders are liabilities to the proprietor; thus, the accounting equation become:

$$\text{Residual Equity} = \text{Assets- (Liabilities + Preferential shareholders)}$$

The proprietary theory represents the agency relationship between managers and their responsibility towards shareholders. Van Mourik (2014) connotes that, in the agency theory, managers are the agent of the shareholders, and they must make decisions to maximize their wealth. Therefore, managers must ensure they utilize their decision-making role to increase the net assets of shareholders. Shareholders use financial statements to evaluate the performance of both the firm and management (Shun-Chuan, Ying-Chan & Yang-Jung, 2016). Since managers are the agent of the shareholders, they gauge financial performance of the company with management efficiency.

To make decisions, managers need information, financial or non-financial. The most essential information comes from financial statements. Thus, it would be correct to argue that financial reporting is a service function of good decision-making. Financial reporting gathers and processes accounting information to help in making better decisions (Pyzoha, 2015).

The income and determination using the asset and liability approach help investors and managers in the valuation of a firm. This argument is consistent with Sherman and Young (2016) who argued that the asset and liability determination of revenues is the byproduct of valuation of assets and liabilities. It represents the most rational way that can be used to quantify the increase in net assets. It is essential to distinguish the interest of shareholders from those of debt holders in the proprietary theory; this will eliminate potential conflict of interest between shareholders and debt holders.

Social Theory, Enterprise and Entity Theory

According to the entity theory, financial transactions should be analyzed based on their impact on financial statements; this is consistent with the accounting reporting standards that prepare accounting reports based on their impact on the firm. For instance, the statement of financial performance is prepared to analyze the performance of the company over a given period. This information is critical to managers because it helps them to make future decisions based on past performance (İBİcİoglu, Kocabiyik, & Dalgar, 2010). After a company prepares financial statements, managers establish whether sales have increased or decreased during the accounting period. Consequently, they make decisions regarding their marketing strategies and reduction of product cost. For example, if a company makes losses in a certain financial year, managers can analyze financial statements to establish what happened. In this case, the income statement can help managers to establish the result of decreasing profits. A decline in revenues could be a result of declining sales. Through financial reporting, managers make strategic decisions that ensure maximization of the wealth of shareholders.

Analysis of the topic

Financial reporting is an essential ingredient for proper decision-making. This information is prepared through a wide range of different information to help users to make informed decisions. It is possible to establish the quality of a company by examining its financial information. The financial reports help managers to establish the profitability, efficiency, and risk profile of the company. Thus, financial reporting allows both managers and investors to make informed decisions (Luft, Shields, & Thomas, 2016). For instance, investors can use financial statements to compute ratios that will help them to identify the level of financial risk facing a particular firm. It is impossible for managers and investors to determine if a firm is highly leveraged without looking at financial reports. They obtain figures from the balance sheet which are computed to establish the financial risk of business. This way, investors can be able to make the right decisions whether to invest in a particular business or not.

Financial reporting also helps managers to make investment decisions (Stamenkovic & Pavlovic, 2011). Before managers can determine whether to purchase or to replace assets, they must go back to financial statements to establish whether the firm has adequate capital to meet that kind of investment. Therefore, it is arguable that managers and investors rely on financial statements to make decisions. The information present in financial statements acts as a guide to managers when they make investment decisions.

Conclusion

Financial reporting is an essential part of management decision making. It helps both managers and investors to establish the financial risk of a business. Managers can be able to obtain information directly from the financial statement or use other methodology to make decisions. For instance, managers can compute ratios from the balance sheet to establish whether a company is financially healthy. Proper financial planning has to take into account all the strength and weakness of the company. Financial analysis identifies good characteristics of the company so that they can be used to pin-point the weakness of the company to take corrective actions. The importance of financial reporting to can be explained by different literature theories such as proprietary theory, social theory, and enterprise theory. According to the proprietary theory, financial reporting record transaction and events for their immediate impact on the proprietor. It argues that financial statements are prepared from the proprietor's perspective to help in decision-making. The condensed statements that can help managers to make strategic decisions are registered in financial ratios. These ratios help companies to measure their business quality. Different ratios value different business qualities such as profitability, financial leverage and management efficiency. In that context, we can conclude that financial reporting is critical in decision-making. It can also be used to establish the business quality by creating assumptions for successful businesses.

References

[1] Akgün, A. İ. (2016). Quality of the financial reporting within the IFRS: Research on determining the attitudes and evaluations of financial information users. *Journal of Accounting & Finance*, 169-187.

[2] Eng, L. L., Sun, L., & Vichitsarawong, T. (2014). Are international financial reporting standards–based and U.S. GAAP–based accounting amounts comparable? Evidence from U.S. ADRs. *Journal of Accounting, Auditing & Finance*, 29(2), 163-187. doi:10.1177/0148558X1452121.

[3] İBİcİoglu, H., Kocabiyik, T., & Dalgar, H. (2010). Financial statement utilization during decision-making process in smes: a comparative study on European and Turkish managers. *Marmara University Journal Of The Faculty Of Economic & Administrative Sciences*, *28*(1), 209-226.

[4] Li, V. (2016). Do False Financial Statements Distort Peer Firms' Decisions?. *Accounting Review*, *91*(1), 251-278.

[5] Luft, J., Shields, M. D., & Thomas, T. F. (2016). Additional Information in Accounting Reports: Effects on Management Decisions and Subjective Performance Evaluations Under Causal Ambiguity. *Contemporary Accounting Research*, *33*(2), 526-550.

[6] Pyzoha, J. S. (2015). Why do Restatements Decrease in a Clawback Environment? An Investigation into Financial Reporting Executives' Decision-Making during the Restatement Process. *Accounting Review*, *90*(6), 2515-2536.

[7] Rahimi-Laridjani, E., & Hauser, E. (2016). The New Global FATCA: An overview of the OECD's common reporting standard in relation to FATCA. *Journal of Taxation of Financial Products*, 13(3), 9-47.

[8] Sherman, H. D., & Young, S. D. (2016). Where Financial Reporting Still Falls Short. *Harvard Business Review*, *94*(7), 76-84.

[9] Shun-Chuan, C., Ying-Chan, T., & Yang-Jung, L. (2016). Beyond objective knowledge: the moderating role of field dependence–independence cognition in financial Decision-making. *Social Behavior & Personality: An International Journal*, *44*(3), 519-528.

[10] Stamenković, S., & Pavlović, R. (2011). The role and importance of reporting on money flows for strategic and operational decision making in corporations. *Megatrend Review*, *8*(2), 455-472.

[11] Staubus, G. J. (1952). Payments for the use of capital and the matching process. *Accounting Review*, *27*(1), 104.

[12] Timm Rathke, A. A., de Fátima Santana, V., Costa Lourenço, I. E., & Dalmácio, F. Z. (2016). International financial reporting standards and earnings management in Latin America. RAC - *Revista De Administração Contemporânea*, 20(3), 368-388. doi:10.1590/1982-7849rac2016140035.

[13] Van Auken, H., & Yang, K. (2014). Chinese smes' uses of financial statements in decision making. *Journal Of Developmental Entrepreneurship*, *19*(4), -1.

[14] Van Mourik, C. (2014). The Equity Theories and the IASB Conceptual Framework. *Accounting In Europe*, *11*(2), 219-233.