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Impact of Managerial Capability on the Relationship Between IT Expenditures and Financial Reporting Quality

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1.Introduction

The evolution of information technology (IT), recognized as a crucial strategic capability for modern organizations, has the potential to significantly enhance financial reporting processes and improve the overall quality of accounting information. Organizations increasingly rely on IT to facilitate accurate, timely, and transparent reporting, streamline accounting operations, and support managerial decision-making. However, despite substantial investments in IT across firms, the existing literature consistently emphasizes that such expenditures alone do not automatically translate into improvements in financial reporting quality. Empirical studies reveal heterogeneous outcomes, suggesting that the mere presence of technological infrastructure is insufficient; managerial factors play a decisive role in determining whether IT investments yield tangible benefits. In this context, managerial ability—considered a critical intangible resource—can profoundly influence the planning, implementation, and effective utilization of IT systems. Skilled managers are capable of aligning IT investments with organizational objectives, ensuring that technology supports accurate data collection, processing, and reporting. They can anticipate potential challenges, make informed decisions regarding system integration, and facilitate employee training to optimize the use of IT tools. Therefore, managerial competence is likely to act as a moderating factor, enhancing the effectiveness of IT expenditures and mitigating potential inefficiencies. The primary research problem addressed in this study stems from the observation

that, although firms are increasingly allocating resources to IT, the direct impact of these expenditures on financial reporting quality remains ambiguous and inconclusive. This inconsistency highlights a crucial gap in the literature regarding the mechanisms through which IT investments affect reporting outcomes and underscores the importance of examining managerial factors. Without competent management, even advanced IT infrastructure may fail to produce meaningful improvements in reporting accuracy, timeliness, or reliability. Accordingly, this study aims to provide insights into how firms can maximize the benefits of their information technology investments through effective management, thereby enhancing the impact of these investments on financial reporting quality. By focusing on managerial capabilities, the research sheds light on the conditions under which IT expenditures translate into tangible reporting improvements and highlights the critical role of skilled management in bridging the gap between technological investment and realized outcomes. This perspective offers both theoretical and practical contributions, guiding organizations in leveraging their technological resources effectively to achieve higher quality financial reporting.

2. Hypotheses

The research hypotheses are as follows:

H1: There is a significant relationship between information technology expenditures and financial reporting quality.

H2: Managerial ability moderates the relationship between information technology expenditures and financial reporting quality.

3. Methods

This research is based on a sample of 126 Tehran Stock Exchange-listed companies spanning the years 2013 to 2023 (1386 firm-years), selected using the systematic elimination method. The data for this study were gathered using a library research method and analyzed using EViews version 13 and Stata. Given the panel nature of the data, a dynamic pooled regression model (Panel Data) with a first-order autoregressive component AR(1) was employed, and model estimation was conducted using the maximum likelihood method (BHHH). To assess the classical regression assumptions, tests for normality, multicollinearity, autocorrelation, and heteroskedasticity were performed. To mitigate the influence of outliers, all

variables were winsorized at the 5 percent level. Financial data were extracted from audited financial statements obtained via the Codal website, while stock market data were retrieved from the Tsetmc website. The regression framework employed to examine the study's hypotheses and the control variables was adopted from Mungai & Lee (2024). The dependent variable was measured following Francis et al. (2004). Due to data limitations regarding qualitative indicators of IT capability, IT expenditure was employed as a proxy for information technology capability, while the moderating variable (managerial ability) was measured based on Demerjian et al. (2012). Only measurable control variables with available data were included in the empirical model**.**

4. Results

The results indicate that IT expenditures alone do not have a meaningful effect on financial reporting quality, implying that merely increasing investment in IT does not guarantee enhanced transparency or reliability of financial reports. However, managerial ability serves as a positive moderating factor in this relationship, whereby higher managerial skills and competencies significantly strengthen the effect of IT investments on financial reporting quality. These findings confirm that managers' capability in planning, implementing, and leveraging IT resources is a key determinant in realizing the actual benefits of such investments, directly supporting the study's second hypothesis.

5. Conclusion

The rejection of the first hypothesis in this study may be considered as a reflection of more influential variables and structural complexities within the research context, rather than simply as evidence of the ineffectiveness of information technology. If the goal is to improve financial reporting quality, focusing solely on the level of IT investment is insufficient. Simultaneous and continuous investment in developing managerial competencies, enhancing the technological literacy of financial managers, providing managerial training on the strategic use of data and technology, and establishing incentive systems that encourage managers to leverage technology creatively are essential. The success of companies that have achieved above-average financial transparency through balanced investment

in both “technology” and “management” demonstrates that combining these two dimensions is far more effective than focusing unilaterally on either one.

Keywords: Managerial ability, Information technology expenditures, Financial reporting quality, Accruals quality.