

**THE CREATIVE ACCOUNTING CONCEPT IN THE CURRENT ECONOMIC
CONTEXT APPROACHED FROM DIFFERENT PERSPECTIVES IN THE LIGHT OF
MOTIVATIONS UNDERLYING THE MODELLING OF FISCAL YEAR RESULT**

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Abstract

This article is trying to tackle the relationships which exist between three dimensions of economic reality. The objective of this article is to contribute to the study of determinants of accounting result management. The accounting result management deviates from the accounting principles (honesty, regularity and faithful image) and finds its motivations in the contractual relations between the managers and stakeholders. This is in the legal, not more frame. The appreciation of accounting information players is different, their interests are different. Therefore, the flexibility of accounting rules allowed to the managers is opportunistic. The accounting representation cannot be completely objective, it is more or less subjective, but the freedom of judgment should be based on a high level of ethical sensibility. The ethical side in accounting has something to say about the result management, it allows the result to offer a faithful image.

Keywords: creative accounting, faithful image, result manipulation, taking advantage, deceitful practice

Clasificare JEL : M41 Accounting

1. Introduction

In a world governed by risks and uncertainties, the adequate risk control is one of the most urgent problems faced by the managers, auditors, capital holders, bank institutions, governments, taxpayers and the general public. The use of creative accounting practices increased in many developed countries over the last years, which brings into discussion more and more often the ethical issues, but also the concern for risk fighting.

In specialized literature there is no consensus regarding the definition of creative accounting concept, there are different approaches. In my opinion, creative accounting is the result of flexibility which exists in the accounting regulations and which, if they are applied with good faith, allow the assurance of a faithful image of the financial position and performances of economic entities. Each user of accounting information has a certain need, has certain interests and many times, the flexibility offered by accounting referentials is used to satisfy some private interests to the detriment to public interest legally, not morally in situations which privilege a limited number of accounting information users, to the detriment of the majority. The continental accounting system considers that creative accounting is an obstacle to the realization of faithful image, being a deceitful practice, deprived of ethics and unwanted, while the Anglo-Saxon accounting system proves greater flexibility and appreciates creative accounting as necessary for keeping abreast of economic, social and legal evolutions

2. Positive and negative aspects of creative accounting

The concept of creative accounting is accompanied most of the times by a negative connotation. Most of definitions given by professionals present creative accounting as a mechanism of manipulating the information presented in the financial statements, with the main purpose of misleading the investors or state authorities. Thus, the financial statements are drawn up for the purpose of answering the desire of managers regarding the financial position and performance of the company. This involves either the use of accounting methods which lead to fictitious increase of profit for an economic entity (for attraction of new investors) or methods which, on the contrary, privilege the display of modest results (the purpose is to pay lower taxes).

Apart from the opinions which present creative accounting in a negative light, there are also other points of view according to which it is a beneficial technique which aims at finding solutions for the newly appeared problems in accounting for the purpose of presenting as faithfully as possible the financial position and performance of an entity. It is also recognized that this creativity of accountants stimulates the evolution of accounting and implicitly leads to economic and social progress. In fact, one of the manifestations of accounting creativity, which is professional reasoning, finds its consecration in the very accounting norms which require that when the application of norms is not sufficient for a faithful reflection of reality, one should derogate from the norms by applying professional reasoning.

This flexibility in the normalization of accounting envisages the fact that the accounting truth is not the truth of “reflection” kind, but it is rather a “constructed” truth.

3.Factors which generate the need of accounting creativity

We can distinguish a few factors which generate a certain need for accounting creativity such as: the financing need given by the insufficiency of own funds, the intensity and pressure of competition in the context of economic crisis, the degradation of financial situation of the entity and its economic results, the high pressure which comes from investors and analysts to communicate “cosmetized” results, the insufficiency of accounting norms, the heterogeneity of referentials, the harmonization uncompleted yet all transpose in a freedom and opportunism made available by the normalizing bodies.

4.The most common accounting techniques of fiscal year result manipulation

Depreciation of tangible assets policy

a. The option for one or another depreciation methods of an asset, during its useful life, has a different impact in time on the result, depending on the scheduling by periods of expenses with depreciation. Thus, different depreciation methods have a different impact on the result, depending on the method chosen we modify the distribution in time of expenses with depreciation: - the straight line depreciation method leads to constant expenses with depreciation during the useful life; - declining-balance depreciation is materialized in a decreasing expense with depreciation during the useful life; - accelerated depreciation leads to higher expenses in the first year, with effect on reduction of result and even expenses for the remaining period.

b. Different options on the useful life lead to different expenses with depreciation, respectively different images on the result. The revision of useful life leads to adjustment of expenses with depreciation corresponding to the current and future periods. The deduction of residual value has the effect of reducing the depreciation and therefore, increasing the result of fiscal year.

Stock evaluation methods

The influence of stock on the subjective or objective attitude is quite high, if we consider the possibilities of option of the current fiscal year or the next year in some cases, if refer to their over-evaluation or under-evaluation.

a. The inclusion in stocks of dead or morally worn out stocks represents a manipulation method. If the dead or worn out stocks are removed from management, the expenses will be affected which has consequences on the result, it diminishes the result. At the opposite pole, the company management may manifest an optimistic attitude and consider that these “dead” stocks can be valorized, especially in case of appearance of an economic recession. Different stock evaluation methods at exit lead to different images on the result, in inflationist periods, the use of FIFO and LIFO methods has the following impact on the profit and loss account: - FIFO – the evaluation of exits is made at the lowest prices, and the evaluation of final stocks at the highest prices, which leads to an increase of operating result and implicitly an increase of profit tax; - LIFO – evaluation of exits is made at the highest prices and the final stocks – at the lowest prices, which leads to a reduction of operating result, and implicitly a reduction of profit tax. In the price reduction periods, the situation is reversed. The result suffers changes depending on the change of stocks evaluation method at exit.

b. The inclusion or non-inclusion of expenses in the stocks acquisition cost creates opportunities for subjectivity and creative accounting. If the company management manifests an optimistic attitude for the result, it will proceed to the inclusion of more expenses in the production cost and if it intends to reduce the result, with the purpose of paying lower taxes to the state budget, it will eliminate a series of expenses from the production cost.

c. The inclusion of financial expenses in the production cost of stocks has the effect of increasing the result in the fiscal year when the expenses are included. At the opposite pole, if the company management has a pessimistic vision on the result, it will apply the result method treating the interests as expense element of fiscal year result.

d. An error voluntarily noticed in determination of the size of existing stock in patrimony at the end of fiscal year can lead to a „flattening” of the result, meaning that the underevaluation or over-evaluation of the final stock has an impact not only on the financial statements of the current year, but also on the financial statements of the next year.

Lease-back operations

IAS 36 requests that at each date of the balance sheet, it establishes whether there are hints that an analysed asset has suffered depreciation. A subjective management estimates that there are no clues of asset depreciation, thus avoiding the reduction of result by a potential expense with depreciation. If it estimates that the recoverable value is lower to net book value, the asset will be considered depreciated for difference and the result will be reduced by the

expense with depreciation. At the opposite pole, if the company management has an “optimistic” attitude on the result, it will appreciate that there are no clues that the asset suffered depreciation, thus avoiding the reduction of result. The lease-back operations (lease-back operations consisted of sale of an asset and its immediate takeover in location) have as impact the highlighting of a surplus value which will be acknowledged in the selling year in results. The royalties will be recorded during the leasing agreement period. By treating it as operational leasing we avoid the observation of a debt and reduce the indebtedness degree.

Provisions

The foundation, increase and reduction of provisions must be done with discernment, prudence and foresight by the management. Thus, it can represent a chance to flatten the result. The overestimation of provisions in the years with high profit leads to the reduction of result and the write-back of provisions in the years when the company has deficit leads to increase of result, both cases influencing the determination of profit taxation.

Contracts in constructions

The choice between the two accounting methods of the construction contracts has the following impact on the profit and loss account: - based on the completed contract, the result will be recognized at the finalization of contract; - based on the completion percentage method, the result will be scheduled in time for the whole agreement period. The passage from one method to another also has a significant impact on the profit and loss account.

5. Conclusions

From my point of view, creative accounting represents the instrument created for supporting the managers; it is used for the promotion, and support of company image and with the purpose of selecting the information so that the data offered supports the interest pursued. Thus, even if the use of creative accounting is not an illegal option, it reveals that managers, being under financial pressure, will look for solutions, without even considering the observance of ethical standards. In other words, the truth said only in half and the lie could be susceptible of possible frauds. The existence of accounting options on the background of the freedom of estimation and choice allows the company management, depending on the interests pursued or even the inclination to optimism or pessimism, to reverse reasoning or transpose in accounting legal, financial and economic innovations, for which they could not find solutions from normalization point of view; thus, they can create certain opportunities for subjectivity and creative accounting; this can have as effect the modelling/cosmetization of result and the content of financial statements. It is noteworthy that these procedures contain a “dose” of accounting creativity with subjective nature, and although they change the presentation of accounts, they are the result of an option chosen from several methods, which makes us state that they fall within the perimeter of accounting regulations. If the goal of creative accounting is assumed to improve accounts (or the image they give to economic entity), taking advantage of the weaknesses and shortages of accounting regulations, we think that this concept is not new, because the options principle has been known to the accountants for a very long time.

6. Bibliography

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