

**FUNDAMENTAL ETHIC PRINCIPLES OF THE
ACCOUNTING PROFESSION AND CONFLICTS OF INTEREST IN
THE SECTOR OF SMES**

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Abstract

We speak nowadays more and more about the role of SMEs from our country in the development of the Romanian economy and the importance of this sector in the development of society and the knowledge economy. As it is in peak maturing process, this sector is still a fragile sector, affected by economic struggles and suffering from chronic underfunding and economic stress.

The generalized crisis that has forced Romanian SMEs to evolve in a hostile economic environment, characterized by structural unbalance, by fiscal instability and a banking system reserved at granting credits for small companies, has left long term marks.

In this context, less favorable to the development of the SMEs sector, we believe the approach of this issue is timely and opportune with a view to the reality in our country.

All professions are subject to laws, norms and regulations, and it is also the case for the accounting profession, which requires also elaborating a code of deontology. This code represents a declaration on the values and principles guiding the daily activities and practices of professional accounting representatives. The code of deontology comprises the application rules that must be followed by accountants in order to conform to the standards and their specific usage.

The accounting profession – a regulated profession

a) The necessity of regulations

The professional authority must regulate the activities and behaviors of its members in order to ensure the fact that their responsibility towards the public

interest is accomplished, including the cases when there exist important external regulations from a governmental agency.

b) **The coverage and quality of the regulation:** the requirements for access, certification or authorization, the requirements regarding continuous learning, the monitoring of professional accountants, the ethic and professional standards that the accountants must follow, the disciplinary procedures and systems in case the professional accountants do not follow the above requirements.

In order for the regulation to ensure the fact that the accounting services respect the highest standards, it must itself obey the public interest, be proportional, transparent and non-discriminatory, it must respect competition, be precise, segmented according to target and implemented in a consistent and just manner, and revised periodically.

c) **Means to implement the regulation**

There are three means of implementation of regulations:

- *self-regulation*, specific to liberal economies: the professional authority is recognized by the government, which also grants it the responsibility to manage the profession's regulations
- *external regulation*, the profession is regulated by the government, either through a governmental agency, or through an independent one with regulation responsibilities;
- *co-regulation*

d) **The regulation of the accounting profession at European level**

The profession is being subject to the "Directive 89/48/EC", replaced by the "Directive 2005/36/EC" regarding the recognition of professional regulations.

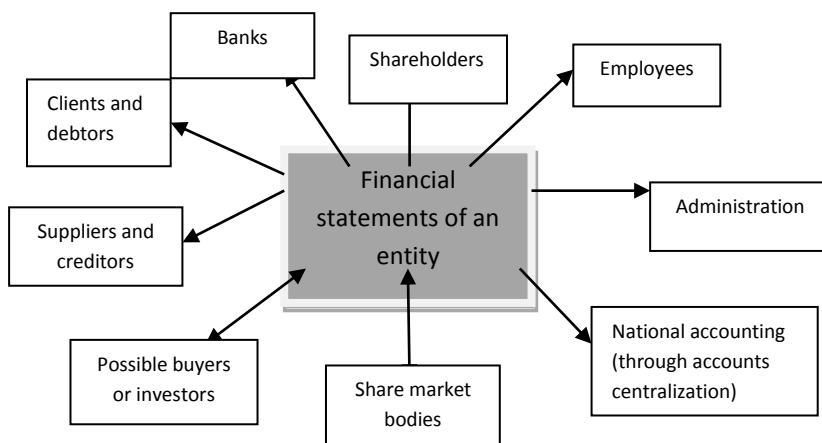
Special regulations

Due to the importance of the statutory audit as final activity that filters the flows towards the consumers (users) of the information contained in the financial statements of an entity, the additional requirements regarding this activity and the circumstances for authorizing the statutory audit providers (individuals and legal entities) are being regulated by a distinct Directive, 84/253/EC, also known as the 8th Directive, replaced by the Directive 2006/43/CF, also known as the new 8th Directive.

The role of the accounting profession

a) **Satisfying public interest**

The accounting profession distinguishes itself from other professions, among others, through the responsibility towards public interest and towards all other parties interested in the activities undertaken by the entity: shareholders, employees, suppliers – creditors, banks, administration, national accounts, share market bodies, investors, etc.



b) Economic development

There is no human progress without the development of markets, and markets cannot develop without accounting professionals; therefore accounting professionals satisfy a general interest.

The accounting rules, as well as the main actors – accounting professionals -, are indispensable for the progress of world economy. All accounting professionals have the mission to respect public interest, and this task must be accomplished regardless of the place of activity: in public institutions, in business, in education or as freelancers.

The role of satisfying public interest by the accounting activity and professionals for the sustainable economic development is conditioned by the existence of strong national professional authorities, which would enforce international standards in the field of accounting and audit.

The accounting profession between regulation and public interest

Accounting and the activities that require accounting knowledge are commercial activities, and the consumers must choose freely among the suppliers of such services; therefore the accounting profession is a liberal

profession, and the professional authorities –regulating authorities- have been from the very beginning the guarantor of serving the public interest.

The Code of Ethics for Professional Accountants and authorized accountants of Romania, from 23.10.1995, published in the Monitorul Oficial (Official Gazette), Part I No 276 of 27.11.1995

The fundamental principles that must guide the professional accountants in their activities and professional relations comprise the following:

- a) **Integrity.** The professional accountant must be honest, fair and sincere in his or her activities.
- b) **Objectivity.** The professional accountant must not succumb to prejudices or preconceived concepts that may affect his or her objective thinking.
- c) **Independence.** When the professional accountant acts as freelancer, it must also be free from any interests that may bias his integrity and objectivity, no matter what the reality is, such as:
 - ✓ direct or indirect financial involvement in the activities of a client, for example: accepting payment, owning participations to the capital, lending or borrowing goods, services or money, granting or receiving warranties or securities from or to his or her clients;
 - ✓ the involvement of the professional accountant in the activities of a client, as member of the executive board or as its employee;
 - ✓ trade acts or jobs performed in the same time as a freelancing profession, that might involve a conflict of interest, or which are incompatible or contrary to the liberal performance of the accounting profession, or which are incompatible with the requirement to display independence, integrity and objectivity;
 - ✓ the impact of personal and family relations on the independence;
 - ✓ the cases when the fees received from a client amount to a high and unacceptable percentage for the total turnover of the consultancy company or of an individual practitioner; this requires that most of the professional accountants do not perform consultancy acts for a single entity or commercial company;
 - ✓ accepting to perform activities based on unclear fees, which had not been previously clearly established through contract or convention.

The list of incompatibilities to the independence of the accounting profession is not exhaustive and all members of the Body must foresee the situations that may affect their integrity, even if they have not been expressly mentioned above.

Examples – The difference between conflicts of interest and incompatibilities

One of the most frequent problems that occur in the administrative system, as well as the mass media, is the confusion between conflict of interest and incompatibilities. While, in order to speak about conflict of interest, the public persons must take a decision that influences a personal interest, the situation of incompatibility of a public official does not require any decision, and it is considered sufficient that they occupy at the same time two or more positions whose association is forbidden by the law.

Example of conflict of interest:

The mayor A from town X signs a contract with his wife's company. Or the Local Council B organizes a public tender which is won by the council president's brother.

Example of incompatibility:

Vice-mayor X holds at the same time also the position of member of administrative board of a local national autonomous company or a firm operating under the supervision of the Local Council.

- d) **Professional competence and interest:** which involves the constant updating of the theoretical and practical knowledge. This principle requires that the accounting professional holds the necessary skills specific to the mission that he or she has to perform and accomplishes the two requirements of the concept: the acquisition and development of skills.

CONFLICTS OF INTEREST: definitions and examples

Although there is a well-defined code of ethics for:

- ✓ liberal professions from the economic field, such as: the Body of Expert and Licensed Accountants of Romania (CECCAR), the Group of Expert Legal Accountants (GEJ), Financial Auditors (CAFR), Financial Consultants (CFA), and Evaluators (ANEVAR);
- ✓ public officials (under the law 188/1999 with subsequent changes and additions).

there are many cases when conflicts of interests occur.

A public official finds himself or herself in conflict of interest when, from his or her position of public official, he or she makes a decision or takes part in a decision making process which involves a personal interest.

The recommendation 10/2000 of the Committee of Ministers of the Council of Europe includes a definition of conflict of interest for public officials, in article 13, as follows: *Conflict of interest arises from a situation, in which the public official has a private interest which is such as to influence, or appear to influence, the impartial and objective performance of his or her official duties. The public official's private interest includes any advantage to himself or herself, to his or her family, close relatives, friends and persons or organizations with whom he or she has or has had business or political relations. It includes also any liability, whether financial or civil, relating thereto.*¹

According to the OECD², the conflict of interest involves a conflict between the duty towards the public and the personal interests of a public official. The conflict of interest occurs when the public official's interests influence or might influence from the point of view of the private person the fulfillment of the official obligations and responsibilities.

We can analyze the component parts of this definition as follows:

1. *Participation to decision making* – this condition is being fulfilled when the decision depends exclusively on the will of the respective public official, but also when the action of the public official represents only a part of the decision making process. The case is valid also when the public official is part of a collective authority which makes decisions by voting processes, and the official takes part in the debates and the voting act.
2. *The existence of a personal interest* – can be represented by a benefit that the public official or a close person may obtain as a result of the decision. Therefore, in order for the conflict of

¹ Recommendation No.R (2000) 10 of the Committee of Ministers to Member states on codes of conduct for public officials, disponibil la adresa web <https://wcd.coe.int/wcd/ViewDoc.jsp?id=353945&Site=CM>

² Managing Conflict of Interest in the Public Service, disponibil la adresa web <http://www.oecd.org/dataoecd/17/23/33967052.pdf>

interest to be valid, the public official must take part in a decision making act that affects a personal interest.

Types of conflicts of interest:

The conflict of interest can have different forms, as follows: it can be potential, actual or consumed. The potential conflict is when a public official has personal interests that may generate a conflict of interests in the case a public decision needs to be taken.

The potential conflict of interest: X is the chief architect of town M, and his brother is the director of a large construction company. The conflict of interest occurs when the official has to make a decision that might bring an advantage for one of his close ones or for one of the business partners.

The actual conflict of interest: X is the chief architect of town M, and his brother's company has applied for obtaining a building permit in that town.

There is also a third type, the consumed conflict of interest, when the public official participates to the decision making act where he or she may hold a personal interest, which is against the law.

The consumed conflict of interest – X as chief architect of town M has signed the building permit requested by his brother's company.

The expectations of the public regarding the behavior that must be displayed by the public official vary depending on the actual type of conflict of interest at a certain moment in time. While in the case of potential conflict of interest, the required behavior from the official is rather to perform his tasks in a transparent and objective manner, in the case of actual conflict of interest, the official must refrain from making any decisions, and inform his superior regarding the situation. The consumed conflict of interest occurs when the official has not refrained from taking a decision when he was in actual conflict of interest, and requires sanctions according to the

According to the Romanian law:

I. Criminal law

The Criminal Code – article 2531 – the competence of the Prosecutor's Office attached to the Court of Appeal: the act of a public official who, in the exercise of his public authority performs an act or participates to the making of a decision which results in the direct or indirect material benefit for himself or herself, or his or her spouse, relative or in-law up to the 2nd degree, or for a third party with whom he or she has been in working relations over the past 5 years or from whom he or she receives services or any type of

benefits, is punishable with imprisonment from 6 months to 5 years and the exclusion from any public positions for the maximum period foreseen. The provisions of paragraph 1 do not apply to the issuance, approval or adoption of legal acts.

1. *The obtained benefit is exclusively material.*
2. *The group of people for whom the benefit can be generated is circumstantial.*
3. *In the jurisprudence, the procedures regarding legal acts have been constantly excluded from the provisions regarding conflicts of interest. This is because of the nature of legal acts: they have a general applicability, which means they include norms referring to the behaviors of a category of individually determined suspects.*

Other connected crimes from the Law 78 of 2000 – competencies of the National Anticorruption Directorate:

Art. 12 – The following deeds are punishable with imprisonment from 1 to 5 years, if executed with the view to wrongly obtain any goods or benefits for oneself or for another:

- a) *performing financial operations, such as trade acts, incompatible with the position, tasks or activities performed by a person, or concluding financial transactions using the information provided by the position, tasks or activities performed;*
- b) *using, in any way, directly or indirectly, the information not destined for the public, or allowing unauthorized persons to access this information.*

Art. 13 – The deed of the person that owns a management position in a party, syndicate, association of employees or a non-patrimonial legal entity, of influencing or using his or her authority with the aim to obtain for him(her)self or another undue money, goods or any benefits, is punishable with imprisonment from 1 to 5 years.

II. *Administrative law – competencies of the National Integrity Agency*

Art. 72 of Law 161/2003, book I, title IV, chapter I:

1. *The person that holds the position of member of the Government, State secretary, deputy secretary or connected positions, prefect or vice-prefect is forbidden to issue any administrative act, or any legal act or participate to any decision making act from his or her public position that results in a material benefit for him(her)self, his/her spouse or first degree relatives.*

2. *The obligations from par. 1. do not refer to the issuance, approval or adoption of legal acts.*

Art. 76 of Law 161/2003, book I, title IV, chapter I:

1. *Mayors and vice mayors, general mayors and vice mayors of Bucharest are forbidden to issue administrative acts or legal acts or dispositions, from their administrative position, which produce material benefits for him/herself, his/her spouse or first degree relatives.*
2. *The administrative or legal acts or dispositions issued under the conditions of par. 1 are void.*

Art. 47 of Law 215 from 2001:

1. *The local counsellor who, through his/her spouse, in-laws or relatives to and including the fourth degree, has a material interest in the matter discussed by the Local Council, is forbidden to take part in the debate.*
2. *The decisions adopted by the Local Council that infringe the provisions of par. 1 are legally void. The nullity is declared by the Court of administrative law. The action can be brought forward by any interested party.*

Art. 79 of Law 161/2003, book I, title IV, chapter I:

1. *The public official is subject to conflict of interest if he/she finds him/herself in the following situations:*
 - a) *is requested to make a pronouncement regarding any demands, or to take any decisions or participate to the decision making which influence legal entities or individuals with whom he/she has material relations;*
 - b) *takes part in a commission according to the law, together with other public officials who are his/her spouse or first degree relative;*
 - c) *the material interests of his/her spouse or first degree relatives can influence the decisions that he/she must make when performing his public duties.*

We emphasize the fact that the definition of conflict of interest in the administrative sphere is, in most cases, more restrictive than in the criminal sphere (in criminal law, the conflict of interest is punishable up to the second degree relatives, while in the case of administrative law, only to the first

degree). There is an exception regarding the local and district counsellors, where the coverage reaches up to fourth degree relatives. This situation was a result of the unwillingness to reform the notion of conflict of interest at the time when the National Integrity Agency Law was passed. For the criminal cases, when the provisions of art. 2531 or other special crimes are valid, the criminal law has priority over the administrative law. Actually, the National Integrity Agency Law expressly foresees that the integrity inspectors must alert the prosecutors when their findings indicate the existence of a crime.

CONCLUSIONS:

It is certain that a healthy society relies upon clear laws, norms, regulations and procedures, but their application is, indeed, directly influenced by the professionalism and ethical behavior of those who enforce them, and, as we have seen above, the importance of the professional accountant is great, regardless of the hierarchical position in a small or medium sized company.

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