THE IMPACT OF CREATIVE ACCOUNTING ON THE PREPARING AND PRESENTATION OF FINANCIAL STATEMENTS

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Abstract

In a world governed by the rules of the market economy, the importance of information, and of their handling in the decision making process is continuously growing. This is a result of using the creative accounting as a method of "grooming" the accounting information.The need for information is growing and data have to be offered faster and to be more diversified. In this context, the accountant has to make available to the decision-makers the necessary information without waiting for standard-setting, thus the call for finding creative solutions that offer advantages to companies, under the conditions laid down by law. These solutions are varied, but all of them try to change the image of the results of a company. The creative accounting becomes a necessary management tool and it is used in order to promote the image of a company. Therefore, a selection of information is necessary in order to pursue its legitimate interests.

This paper intends to analyse the creative accounting techniques and the ways in which it can impact the information included in the financial statements.

Keywords: creative accounting, financial statements, company,information

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1. Introduction

The problems faced by a company in a world that is increasingly complex as a result of conditions imposed by competition still strong, the quest of profit maximization, taking of the best possible decisions related to the leadership activity, bring to the fore the role that the information provided by the accounting statements have in making these decisions. In these conditions, creative accounting is increasingly often mentioned

Although still in the early 20's began to be used as a way of ”handling of accounts”, and over the years has been called ”the art of presentation of the balance sheet” (Gounin), ” the art of to calculate the benefits” (Ligon) or ” the art of faking a balance sheet”(Bertolus), in the last time find more often the present techniques of manipulation of accounting information, financial scandals being witnessed in the use of these engineering accounting.

The literature has tried to identify the the reasons for using accounting creative, among them being: the process through which accounting professionals use their knowledge in order to manipulate the figures included in the annual accounts or the process by which transactions are structured in a manner that to allow obtaining the result accountant wanted (Naser K.); the manner in which management uses certain deficiencies or ambiguities in the wording of the accounting rules with the aim of presenting a certain image image of the financial performance (Shah A.C.); improving the information provided to investors (Trotman M.); the manner by which it allows the accounting to keep up with the development of the growing markets and with the proliferation of financial products (Malciu L.); the result of the flexibility that exists in the accounting regulations and that, if applied in good faith, allow us to provide a true picture of the financial position and performance of economic entities (Grosanu A.), recognizing, however, that the flexibility it provides the referentials accounting it is used for the satisfaction of private interests, at the expense of the public interest.

Regardless of the definition of time accounting creative, it uses a set of procedures which have as their objective the change in the level of the result, be in order to optimize his, be in order to minimize its financial statements. The procedures used are based on accounting regulations prerequisites, that use, however, of the shortcomings of the accounting rules and of the mechanisms that accounts put them at the disposal of the professionals to intervene on the information that you submit financial statements.

These processes may have the effect be shaping the outcome and decisions of the management taken within the company, be improvement the information presented in the balance sheet or in the account of the results. All are based on the achievement of quantification more or less accurate, which may thus influence results published. Also the information presented in financial statements is synthesized with the help of economic and financial indicators, but their choice is most often subjective, the companies being tempted to manipulate figures, thus establishing a direct causality between the indicators presented and the accounting information.

And then, if we were trying to find answers to the question about the use of creative accounting, the answers would be related to: the need to finance equity where insufficient own funds are available; the need to respect the indicators imposed by financial institutions; degradation of results and financial situation; Economic situation imposed by the economic crisis; increased pressure from investors and analysts; and let us not forget that the lack of accounting rules, the heterogeneity of referentials and the ongoing harmonization that allow for the freedom of decision-making allow the implementation of creative accounting.

Freedom of choice of accounting policies by entity management, leading to an increase or decrease in the result is one of the main information limits of the profit and loss account.

2. Creative accounting techniques

Creative accounting techniques act on fixed assets, current assets, and equity and debt. Considering that the balance sheet is the expression of the presentation of the double assets, it is obvious that the creative accounting techniques related to the fixed assets will in some cases affect the size of the equity or the debts, and then influence their influence on the information presented in the results account.

We will, in turn, analyze these accounting information manipulation techniques.

Creative accounting techniques for fixed assets refer to the treatment of development expenses, the fund, formation expenses, revaluation, depreciation policy and depreciation adjustments, capitalization of post-commissioning expenses and interest.

Treatment of development expenditures is related to the decision to capitalize or not the expenses, the capitalized expenses and the depreciation policy. The distinction between development and research spending creates prerequisites for the manifestation of accounting creativity. Thus, an entity using a capitalization policy for development costs may increase or decrease the result of an exercise by simply reclassifying it into the research category, in which case the profit or loss account or the development category is affected, in which case The balance sheet is affected. Furthermore, the entity may invoke at any time uncertainties about the completion of the project to transfer the expenses on the balance sheet to the profit and loss account.

Capitalizing the commercial fund and depreciating it over its useful life influences the outcome of future exercises. Imputation of goodwill on equity affects their impairment and the result of future exercises is not influenced by amortization of goodwill.

With regard to the formation expenses, creative accounting techniques refer to its recognition in the financial statements, as well as to depreciation and amortization periods. Entities may choose whether the budgeted expenses are capitalized on the balance sheet or directly affect the profit and loss account. As regards depreciation, the formation expenses are either carried over to expenses for a period determined by the management of the economic entity or are covered by the capital premiums.

Creative accounting techniques relating to asset revaluation are typically used by entities in difficulty to increase their own capital. The choice of the valued and the timing of the valuation is also relevant to creative accounting.

In terms of depreciation, this is based on depreciation, amortization and depreciation. The depreciation period is an accounting estimate available to the management of the economic entities, thus having a subjective use in view of the fact that economic use is set within a range of normal operating time, and the choice of this period may be when the results are recorded economically different.

Moreover, the duration of economic use is an accounting estimate that can be changed after the start-up of fixed assets, which generates changes in accounting depreciation with all that this implies on the result of the exercise.

In order to avoid these pitfalls, external users have to calculate the gross operating surplus, an indicator that does not take into account the depreciation and provisioning policy, being appreciated as the purest indicator of economic performance.

If there is a recoverable amount of property, plant and equipment at the end of the financial year, the issue of impairment adjustments is recognized. Although the book value at the date of entry into the entity appears to be objective, in comparison with the recoverable amount, the depreciation recorded in respect of which a number of variables change, thereby altering the final result, must be deducted from the carrying amount.

Another technique of applying creative accounting to fixed assets is lease-back, which involves the sale of an asset to a leasing company, immediately followed by its take-up in financial leasing. In this way, the entity obtains the necessary economic resources for the normal conduct of the business and can also use that asset as it is. Thus, in the year in which the transaction takes place, the result is increased, but will diminish in the coming years. The higher the transaction price, the more lender and higher interest rates will be paid by the entity, but the funding requirement can be covered or a better financial situation can be achieved at this time.

Creative accounting techniques related to current assets refer to: valuation of inventories, volume of stored production, artificial transfer of investment titles, calculation and recording of adjustments for depreciation of inventories and receivables, etc.

As regards stocks, the decision to achieve production, even if it does not have orders for that production, can enable an entity to improve its outcome. This can be done through the management of fixed costs that are included in the cost of production and are not directly settled on the result of the year. Thus, the decision to produce, although not having immediate utility, allows to hide the costs of sub-activity and to obtain a better result.

Accounting creativity can also be manifested in terms of production assessment methods unfinished at the end of the year or stock valuation at discharge. Thus, the assessment can be made using the FIFO, LIFO or CMP method, methods which, under inflation conditions, lead to different results.

Thus, in the FIFO method, the assessment of outputs is made at the lowest prices and the one of the final stocks - at the highest prices, which leads to an increase in the operating result and, implicitly, the profit tax, while in the method LIFO is valued at the highest prices, and the final stocks - at the lowest prices, leading to a decrease in the operating result and, implicitly, the profit tax.

Also, the way of accounting for the cost of the sub-activities used in the management accounting can lead to the manipulation of the results.

Thus, using the full cost method, the production cost includes a share of the annual fixed costs based on the quantity in stock and the annual quantity produced, in which case there is no cost of the sub-activity, with all fixed costs entering the cost of production If production capacities were not used at full capacity.

By using the rational costing method, the cost of production includes a share of the annual fixed costs determined in relation to the quantity in stock and the normal annual production, in which case the costs related to the non-use of production capacity are settled directly on the result without taking into account the cost of production.

In relation to receivables, the entity's risk is related to non-collection. In this respect, claims may be secured, underwriting of insurances allowing the entities to improve the result with the difference between the value of the impairment of the claim and the premium paid. Assurance of the claim may be made after the impairment exercise. Thus, if the company has a high level of profit, it will be interested in making an adjustment for impairment, and when the outcome is unsatisfactory, it will secure the claim by recording the insurance premium and proceeds from the resumption of adjustments.

Creative accounting techniques related to equity relate to: the provisioning policy or capital premiums.

Provisions are funds intended to cover unsafe risks linked both to their timing and to the moment when they will occur, generating either expenditure or revenue. They occupy an intermediate position between equity and debt. Due to the fact that the provisions need to be estimated, they create conditions for smoothing the financial results.

Capital premiums have the role of protecting old shareholders against new shareholders. They represent the price paid by new shareholders to participate in the company's capital. The primary capital destination may be capitalization, increase of reserves or coverage of expenses related to the issue and sale of new shares. Because spending on the issue and sale of new shares is initially recorded as part of the formation expenses, they can be redeemed through creative accounting in the context of those above. Thus, these expenses either amortize and directly influence the outcome, or are covered by the issue premiums. In this case it is considered that this does not affect the interests of the shareholders, but it favors the state because the financial result is higher, and then also the higher profit tax. In this case, however, priority is given to the variation of the result and the less importance of the variance of the capital premiums.

Debt-related creative accounting techniques refer to: different types of product sales or expenses with collaborators.

Thus, with regard to sales, there may be sales within their own units where both the production function and the commercial function meet, and the accounting must report information for each of them. Creative accounting is related to the way in which the expenses are recorded and recorded in the profit and loss account.

The transfer of the goods from the warehouse of the entity to the retail units implies from the accounting point of view their transfer either in the category of goods or in the category of finished products. When goods are recorded as goods, an overstatement of the entity's expenses and revenues occurs. The second variant is more accurate, since it sells its own finished products, quantifying the value of resource consumption and economic reality more accurately.

With regard to sales made to third parties, creative accounting may use situations where sales are based on formal arrangements between the seller and the buyer, whereby the buyer can return to the seller the goods that have not been sold, this is a way to smooth the result in Where the economic performance is inadequate in the year of sale. In this way, income is recognized in the year of sale, and in the following year, when the return occurs, the expenses will be recorded. However, this technique can be eliminated because the annual financial statements are approved after the close of the financial year, in order to be able to identify events and transactions subsequent to the closure of the exercise but which are related to the year ended.

Another example of creative accounting is the collaboration with the authorized individuals in the detriment of the employees, as they are transferred to the profit-making entity at the level of the corporation paying the profit tax. In this case, creative accounting is used to optimize fiscal pressure.

3. Conclusions

Creative accounting is judged by its negative image because it affects the final image requirement of financial statements. This happens when the flexibility allowed by accounting rules is used to make reports in favor of a small number of users, to the detriment of most of them.

Secondly, creative accounting is associated with fraud, but it is legal and can be a factor in touching the true image when it is applied in good faith.

The choice and implementation of accounting policies, the way in which accounting policies are applied are the choices made by professional accountants and often result in damaging the results and financial position reported. Finally, we can say that creative accounting is the process by which transactions are structured in such a way as to enable the desired accounting result to be obtained.

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