

SOME INSIGHTS REGARDING CREATIVE ACCOUNTING IN ROMANIAN ACCOUNTING ENVIRONMENT - REGULATORS, FINANCIAL AUDITORS AND PROFESSIONAL BODIES OPINION

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This empirical study reports the results of a survey designed to explore the existence and magnitude of creative accounting practices in the Romanian accounting environment using as a reference point the opinion of some of the top representative accounting professionals like: financial auditors, regulators and professional bodies representatives of the Chamber of Financial Auditors of Romania and also representative of the Body of Expert and Licensed Accountants of Romania.

Since the existence of creative accounting practices are connected in accounting with issues of vulnerability and in some cases panic getting to know its magnitude can be regarded of higher importance. In this respect we were interested to see if our respondents can document its existence and magnitude based on their experience. In order to achieve this goal our methodology employed neutral and direct interviews based on closed questions questionnaire.

The results of our empirical study documented that the credibility of accounting profession in the Romanian accounting environment is not affected by items like creative accounting since all our respondents asserted that is not facile to employ creative accounting schemes in the practice of accounting. One particular question was concerned about the ease of detection of creative accounting practices. In this respect we interviewed our respondents and all had similar opinions that in order to detect those practice skilled professionals are needed and more than that the desire to engage in this demarche since it is not specified particularly in the law.

When it comes to creative accounting schemes that our respondents could identify in their day to day work they shared similar views: items like profit overstatement and profit undervaluation, income tax and leasing can be included frequently in those schemes. On the other hand practices of creative accounting that include goodwill, provisions and developments costs are not found in a significant proportion in the Romanian economic environment.

Keywords: creative accounting, creative accounting practices, credibility, existence, magnitude

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Introduction

Nothing is more important or more rewarding in the course of preparing and communicating accounting information than the ability to present it to users and in this context the wording "ability" is representative since this profession is based entirely on professional judgment. Accounting is assessed primarily through its capacity to present financial information for the process of decision making. In this respect objectivity of accounting information is crucial since it should be elaborated under the TFV requirements. The above describe the fair accounting part while all the items that are not included in this category were documented as unfair components that made their presence felt increasingly as empirical studies documented their existence through elaborate evidence (Smith 1992:4-221; Mulford and Comiskey 2002, 2005).

Motivation of the study

Instead of extending the importance of such a topic we bring into attention the opinion of Katherine Schipper (1989:91-102) regarding the importance of getting to know earnings management and pointing out the fact that her opinion can be expanded to our entire study area: "Understanding earnings management concerns one of the central questions in accounting". From that point in time and until the present time its opinion becomes even more appreciated even if it was formulated long time ago and referred only to a small part of creative accounting: earnings management.

State of the art

Creative accounting presented under all its forms of manifestation represents a highly debated subject in the literature with old roots in accounting literature in the debating area. Naser (1993:9) asserted in his book *Creative Accounting: Its Nature and Use*, that manipulation of accounts is an old accounting problem that goes back in the 1920s. The trend of examining creative accounting increased over the years and the interest in examining its existence and the taxonomy of its practices also. Sen and Inanga (2009:27-42) asserted in their study also that creative accounting occurrence increased in many developed countries in recent years. Recent developments (Vinnari and Nasi, 2008:97-116) place creative accounting in the public sector too, defying a general wording according to which creative accounting is present only in the private sector. Erickson, Hanlon and Maydew (2006:113-144) discussing on the demand for research in the area of accounts manipulation discussed about the importance of such a topic and also about the legislative and regulatory changes. Earlier empirical studies documented the existence of earnings losses and decreases (Burgstahler and Dichev 1997:99-126), executive compensation and manipulation (Erickson, Hanlon and Maydew 2006:113-144), off balance sheet financing, creative cash flow and goodwill, manipulated development costs, stock valuation methods, income tax and provisions (Mulford and Comiskey, 2002, 2005), accrued income, depreciations and others manipulated items likewise (Naser, 1993).

Methodology

The methodology employed for our empirical study consisted in the neutral and direct interviews based on a series of 18 closed questions addressed to top representatives of the Romanian regulators, financial auditors and professional bodies' representatives.

The motivation for choosing this particular methodology comprised the fact that we wanted to minimize the discrepancies that exists between the declared opinions and the actual behavior (Chelcea, 2001:124). In this respect we wanted to minimize the biases that could occur. By using this particular path we eliminated any freedom to innovate or changing the actual path of research since our scope of the study was to collect the respondent's opinion (Ghiglione and Matalon 1991:77) regarding a predefined set of questions. The main advantages of this instrument are that we had the possibility to observe the nonverbal behavior, to ensure the standardization of the response condition and to collect spontaneous responses.

The closed questions were developed based on Likert Scale rating the items in a group of judges using 1 to 5 rating scale where: 1 can be defined as *strongly unfavorable to the concept*, 2 is *somewhat unfavorable to the concept*, 3 is used when *undecided* rating item is used, 4 is *somewhat favorable to the concept* and 5 is *strongly favorable to the concept*.

The interview lasted from minimum 25 minutes to 80 minutes with a mean of 55 minutes conducted in the workplace of the respondents and one at the Faculty of Economics and Business Administration from Babes Bolyai University from Cluj Napoca. In Appendix 1 we summarized the list of the interviews, the dates and the duration of the interviews, the person who interviewed the respondents.

All our respondents were Romanian citizens based in Cluj Napoca, except one respondent from Bucharest. All interviews were conducted in Romanian language and both researchers took notes during the interviews. No ambiguous answers were received and all questions had an answer.

Research Design

This empirical study conducted in the Romanian accounting environment reports the main results of a survey that used as a research instrument the interview, focused on the perceptions of regulators, financial auditors and representatives of professional bodies regarding the magnitude of creative accounting practices. Since the empirical studies conducted in the literature documented the existence of creative accounting practices in various economic environments (Jones 1991:193-228; Dechow *et al.* 1995:193-225; Burgstahler and Dichev 1997:99-126; Mulford and Comiskey 2002:2-375; 2005:289-303), the Romanian economic environment is also susceptible of being characterized by its incidence. The perception regarding the magnitude of creative accounting practices may depend firstly on the category that we interview: regulators, financial auditors and professional bodies.

In order to explain if that magnitude has the potential to differ in those particular respondents view in practice of accounting we interviewed 8 respondents involved in accounting regulation and accounting practice in Romanian accounting environment. Our sample was not randomly chosen since we were interesting in interviewing some top respondents of Romanian accounting environment and cannot be considered as being a sample that compressed any statistical path that must be followed in the construction of samples used in a research area.

Findings

Our questionnaire contained as we stated before 18 closed questions. The first five questions assessed the credibility of accounting information when taking economic decisions (Q1: *Can one trust the information compressed in the financial statements when taking economic decisions in the Romanian accounting environment*); the ease for a company to employ creative accounting schemes (Q2: *Can be considered facile for a company to employ creative accounting schemes in Romanian accounting environment*); the ease to detect those schemes in general (Q3: *Can be facile to detect creative accounting schemes*); the role of professional bodies and regulators in fighting creative accounting (Q4: *The role of the professional bodies and regulators is essential in fighting creative accounting schemes*) and the role of financial audit in fighting creative accounting (Q5: *The role of the financial audit is essential in fighting creative*). The 13 questions remained tested for the magnitude of some of the most cited items of creative accounting practices or techniques of creative accounting as it is presented in table 2.

The results for the first 5 questions are presented in table 1 as following:

Table 1. Credibility of the accounting information, ease to employ and detect creative accounting practices and the role of regulators, professional bodies and financial audit:

Questions/Respondents	Financial auditors	Regulators	Professional bodies
Q1	FA 1, FA 2 /4	R 1, R2, R3/ 5	PM 1, PM3/4; PM2/5
Q2	FA 1/3; FA 2/4	R 1, R3/ 1; R 2/2	PM 1, PM3/2; PM2/2
Q3	FA 1/2; FA 2/4	R 1, R3/ 2; R 2/3	PM 1, PM3/4; PM2/2
Q4	FA 1, FA 2/4	R 1, R3/ 4; R 2/5	PM 1, PM2, PM3/5
Q5	FA 1, FA 2/3	R 1, R3/ 3; R 2/4	PM 1, PM2/3, PM3/5

Source: Projection of the authors]

When it comes to assessing the answers received for our first question one interesting aspect can be discussed and that is related to the fact that only the professional bodies and the regulators asserted that one can trust fully in the accounting information. In their vision the “financial statements are constructing under the principle of TFV and should be no place for misjudgment” as PM 2 asserted.

FA 1 consider that “ we cannot say that we can trust 100% of the information that is comprised in the financial statement but on the other side we can never say that this particular information is always characterized under the creative accounting influence how some international studies documented”. R2 in this respect admits that accounting information can be manipulated but the incidence is not high. The second question shared contradictory answers as the financial auditors considered that is not difficult to employ creative accounting schemes in the Romanian accounting environment while the latter categories strongly disagree with this. R3 asserted that „ the mirage of creative accounting is beautiful but how much can we talk about creative accounting indeed and how much can we talk about the desire of doing that”. The third question was the only one that received only the strict answers with no additional information on behalf of the regulators. FA 2 asserted that „the detection process of creative accounting schemes must be judged according to the experience of the person that analyzes one accounting item”. PM 1 and PM 4 asserted that is easy to detect those practices “as long as the person that follow this demarche is interested in this” (PM 1) and “you just need the right person to detect them” (PM 3). The role of regulators and professional bodies in fighting creative accounting was considered very important since all respondents were strongly agreed. FA2 declared in this context that “the accounting practices that do not lead to TFV must be inhibited through accounting regulations and that is an ongoing process that never ends”. PM 3 asserted that „everybody must fight creative accounting. I see it only through a spectrum of negativity. We are all responsible for constructing the credibility of the accounting profession and for that reason we all must limit unfair practices”.

The role of the financial audit in fighting those practices was seen as not essential by the financial auditors itself. The latter categories strongly agreed. In this respect PM 3 asserted that “when we discuss about the financial audit and creative accounting the answer may appear as simple, but is complex. We have noticed that every time creative accounting practices are discovered, financial auditors are to be blamed but the truth is that this is not their responsibility to detect that. They must verify for the legality of the accounting information not for items of morality particularly”. Table 6 combined schemes of creative accounting documented in the literature (the references are the ones above). Some of them were presented to the respondents in order for them to assess the frequency that they head or found the item in their day to day work.

Table 6: Schemes of creative accounting and their magnitude in the Romanian accounting environment:

Schemes of creative accounting	Financial auditors	Regulators	Professional bodies
Profit undervaluation	FA 1, FA 2/4	R1, R 2, R3/5	PM 1, PM 2, PM 3/4
Profit overstatement	FA 1, FA 2/4	R1, R 2, R3/4	PM 1, PM 2, PM 3/4
Income tax	FA 1, FA 2/4	R1, R 2/4, R 3/5	PM 1, PM 2, PM 3/4
Depreciation	FA 1/2, FA 2/1	R1/2, R2/1, R3/3	PM1, PM2/2, PM3/3
Provisions	FA 1, FA 2/1	R1, R2, R3/1	PM1/2, PM 2, PM3/1
Goodwill	FA 1, FA 2/1	R1, R2, R3/1	PM1/2, PM 2, PM3/1
Prepayments	FA 1/4, FA 2/2	R1, R 2, R3/4	PM 1, PM 2, PM 3/2
Accrued incomes	FA 1/4, FA 2/2	R1, R 2, R3/4	PM 1, PM 2, PM 3/2
Adjustments	FA 1, FA 2/1	R1, R 2, R3/1	PM 1, PM 2/1, PM3/2
Leasing	FA 1, FA 2/4	R1, R 2, R3/4	PM 1, PM 2, PM 3/4
Development costs	FA 1, FA 2/1	R1, R2, R3/1	PM 1, PM 2/1, PM3/2
Off balance sheet schemes	FA 1, FA 2/1	R1, R2/1, R3/2	PM 1, PM 2/1, PM3/2
Stock valuation methods	FA 1, FA 2/1	R1, R2/1, R3/2	PM 1, PM 2/2, PM3/3

Source: Projection of the authors

As it can be observed from table 6, some of the techniques of creative accounting are present in the Romanian economic environment and as it can be concluded based on their answers in a higher proportion. Those schemes of creative accounting are the ones that include: profit underestimation and overstatement, income tax and leasing manipulations. Other items that are present in a higher proportion (Smith 1992:4-241; Mulford and Comiskey 2002:2-375) in other

economic environments like stock evaluation, off balance sheet, developments costs are somehow inexistent in the Romanian economic environment based on the respondent's answers. When it comes the creative accounting schemes that are developed based on provisions we cannot assert that those are present in our economic environment since none of the respondents declared it as being present. Regarding to this item all respondents asserted that Assistant Lecturers of accounting information don't use provisions even if from a legal point of view they have this possibility. Also none of the respondents declared that they could found in their day to day work an item like goodwill included in a scheme of creative accounting. In this respect PM1 asserted that "I have heard of cases like those where this item was used creatively but I personally didn't found in my work this situation".

Conclusions

In the Romanian accounting environment the credibility is the accounting information has described by our categories of respondents as being high which is not surprisingly since two of the categories are directly responsible for constructing the credibility of the accounting profession. Contrary to the international studies results (e.g. the above cited sources) our respondents asserted that is difficult to employ schemes of creative accounting and the detection process of those scheme involved skilled professionals. The role of regulators and professional bodies is important in limiting its incidence. Profit overstatement and undervaluation, income tax and leasing manipulation are found in the Romanian accounting environment while others techniques of creative accounting that involve goodwill, or developments costs weren't documented by our respondents.

Further developments and scope for future research

Having the fact that this research instrument may offer multiple advantages we intend to use it in our future research but to apply only the interview without combining it with the questionnaire, leaving in this respect room for creativity and also for no influence at all. We intend to use a larger sample and to develop a more robust study at a national level including respondents from each category plus two new categories: Assistant Lecturers and financial analysts. Also from a lack of space we couldn't approach on a higher scale the additional explanations that our respondents gave so in a further study we intend to discuss this part too since that could explain better their opinions.

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Appendix 1 – List of interviewees

Category of respondents	Abbreviation	Duration	Month	Day	Year	Researcher
Financial auditor 1	FA 1	45 min.	Dec.	12	2010	Alina B. Vladu
Financial auditor 2	FA 2	30 min.	Apr.	30	2011	Alina B. Vladu
Professional bodies member 1 (Representative of the Chamber of Financial Auditors of Romania)	PM 1	25 min.	Jan.	18	2011	Adrian Grosanu
Professional bodies member 2 (Representative of the Body of Expert and Licensed Accountants of Romania)	PM 2	70 min.	Jan.	20	2011	Adrian Grosanu
Professional bodies member 3 (Representative of the Body of Expert and Licensed Accountants of Romania)	PM 3	80 min.	Feb.	11	2011	Adrian Grosanu
Regulator 1	R 1	80 min	Feb.	17	2011	Alina B. Vladu
Regulator 2	R 2	40 min.	Mar.	10	2011	Alina B. Vladu
Regulator 3	R 3	65 min.	Mar.	30	2011	Adrian Grosanu

