STUDY REGARDING THE INFLUENCE OF ROMANIAN ACCOUNTING REGULATIONS ON CREATIVE ACCOUNTING TECHNIQUES

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The main objective of this paper is the analysis of Romanian accounting regulations and the identification of the impact they have on creative accounting techniques. Also, we shall investigate the influence some of these creative accounting techniques have on the true and fair value. Basically, we desire to answer the question: to what extent is being affected the true and fair value reflected within the financial statements of a certain entity by appealing to creative accounting. At international level there are several papers having as subject creative accounting, most of them emphasizing the negative role it has upon achieving the true and fait view. The papers that analyze creative accounting techniques in Romania are rather few, reason to start studying the extent to which Romanian accounting regulations allow the use of creative accounting techniques. We shall use the experience comprised within papers published at international level in order to substantiate an objective analysis of creative accounting techniques in Romania and of the impact they have on true and fait view. Being familiar with the creative accounting techniques is equally useful to the entire palette of accounting information users, including the researchers, for one can quantify the positive or negative impact they have on the true and fair value. One can bring suggestions to modify the accounting regulations, if some creative accounting techniques affect the legitimate interests of certain accounting information users. Also, one can perform analyses regarding the situation of this field in Romania in comparison with the existent situation in other countries. The paper's originality is given by the study on the impact of applicable accounting regulations in Romania on creative accounting techniques. There are very few studies in this field in our country and we appreciate that it would be a useful source for the accounting information users. Also, the usefulness of this study is given by the suggestions concerning the instruments to identify the creative accounting techniques that have a negative role on financial statements, so that they would keep their relevance and credibility for the users of accounting information.

Key words: creative accounting, true and fair value, regulations, corporate governance, financial statements, flexibility
JEL CODE: Accounting and Auditing: General M40; Government Policy and Regulation M48

I. Introduction

Specialty literature presents several factors liable to stimulate managers in using creative accounting techniques.

A first hypothesis is the situation in which managers' salaries are calculated according to the accounting result. In this situation they will be tempted to have an opportunist behavior, choosing those creative accounting artifices which allow them to keep these rights to a high level. Therefore, one can meet two situations:

when the results exceed the maximum limit established by means of contract, the surplus will not be registered within current period, but it will be used in the subsequent period when it will be remunerated;
when managers will confront with the opposite situation, finding themselves in the situation of registering great losses, they will apply the method of increasing those losses by including all future probable losses, which will have as a result future superior profits.
According to the creative accounting theories there is a connection between the use of creative accounting techniques and managers' incompetence. A company that has reached an unstable situation will undoubtedly begin to use creative accounting techniques in order to artificially increase profit, and thus, the financial situation to be temporarily concealed. The advantages would be to maintain the suppliers' credibility in order to avoid their refusal regarding the grant of commercial credit or the decrease of credits' refunding period towards financial creditors.
The extremely diverse character of economic activities involves resorting to certain particularities concerning their evaluation, particularities that allow a specific reflection of that certain economic event. The existence of this possibility implies using options for evaluation. Choosing one option or another sometimes relies on professional judgment; therefore, different financial results are obtained according to every accounting specialist's opinion.
Inevitably, the requirement itself of providing the true and fair view can lead to creative accounting, starting from the premise that in order to achieve the true and fair view it is necessary an honest applying of accounting regulations. Sometimes, though, compliance with rules is not enough. Rules cannot be considered a complete code of inflexible rules, replacement of professional judgment. In this sense, the IV Directive explicitly mentions that "when applying an accounting foreclosure is not enough to provide a true and fair view, within annexes one must furnish additional information […] and if, in an exceptional situation, applying an accounting foreclosure is inappropriate for providing a true and fair view to the patrimony, financial situation and result, one must make a derogation from this foreclosure". Therefore, a true and fair view could be achieved only by noncompliance with effective rules, and this derogation may lead to exaggerations and distortions of the reports from financial situations.
One of the elements that may lead to applying some creative techniques may be even the pressure of certain categories of users. An example could be the investors who desire a larger profit in order to raise dividends to more superior values, fact that would induce a pressure upon administrators in this sense.
Because the fixed relationship between cost and expected yield is very volatile for immaterial investments it is very difficult to identify and to measure most of these assets. The problem is even greater as the progressive increase of immaterial investments requires taking them into account in order to define the enterprise. Therefore, this is a favorable field for creative accounting to manifest, having a potential effect of distorting the accounting information in time and space.
Another element that could induce creative accounting, in specialists' opinion, would be the absence or insufficiency of national accounting norms regarding the constitution of social and consolidated accounts. In some authors' opinion (Bernheim, 1993: 58-60, 93), creative accounting practices lean more and more towards a so-called "real management of accounting result" in order to maximize it. According to other authors, besides this objective, creative accounting also aims to increase equity and to decrease the gearing rate (Feleagă, 1996:151).

II.Research methodology

Under the aspect of mainstream research, our paper is oriented to the positivist theory, pursuing to explain through a detailed and thorough approach the different sides of the matter concerning creative accounting techniques in the light of Romanian accounting regulations. We intend to use some elements from the interpretative and critic theories, as a result of approaching different concepts, regulations and practices in this field, in a interpretative and critic manner, following a deduction-based approach. By studying the Romanian accounting regulations one can grasp the applicable creative accounting techniques and their influence on the true and fair value. The limit of this research is the fact that it represents only a fundamental research and it is not complemented with an applicative research which would identify the practical instrument to apply the creative accounting techniques.

III.Creative Accounting Techniques

Creative accounting techniques regarding non-current assets

Creative accounting techniques regarding non-current assets generally refer to the treatment of development costs and of goodwill, to revaluation, amortization policy and impairments, to capitalization of expenses subsequent to commissioning and to interests. For example, creative accounting techniques regarding the development costs are linked to the decision to capitalize or not the expenses, and also to the capitalized expenses' value and to their amortization policy.

The difference between development cost and research costs creates premises for creative accounting manifestation. Thus, an entity that uses a policy of capitalizing development costs can increase or decrease the result of a financial year by simply transferring them within the research category, situation in which the profit and loss account is affected, or within the development category, situation in which the balance sheet is affected. Moreover, the entity can invoke at any time uncertainties regarding the project finalization in order to transfer the development costs from the balance sheet to the profit and loss account (Feleagă & Malciu, 2002: 399).

Creative accounting can also emerge when there are common expenses for several projects, and their delimitation on every project has a subjective character. Also, the dimension of goodwill is easy to manipulate. Thus, the undervaluation of purchased elements determines the increase of goodwill and provides an image of fake profitability in the future.

Creative accounting regarding tangible assets envisages the asset revaluation, the capitalization or not of certain expenses subsequent to commissioning, the amortization policy, and other special transactions.

Amortization policy influences the result evolution by means of three variables: Depreciable cost; Amortization's duration; Method (regime) of amortization (linear, accelerated, and digressive).

In certain countries the depreciable cost is the difference between the input value (historical cost) and the residual value estimated at the end of the period of use. We can observe here a moment in which creative accounting emerges, which is linked to the residual value's estimation and then, at the end of subsequent years, to the revision of this estimation. In Romania, according to the existent accounting regulations, residual value is null, therefore it is not taken into account when calculating the depreciable cost.

Amortization's duration is an accounting estimation available to the economic entity's board, situation which involves subjectivism and, therefore, creative accounting. Within OPFM (Ordinance of the Public Finances Ministry) no. 3.055/2009 it is mentioned that: the amortization of tangible assets is calculated according to a plan of amortization, from the date of their commissioning until the full recovery of their input value, according to their terms of economic use and their conditions of use. The amortization calculated according to its terms of economic use is called financial amortization. Usually, in order for the accounting amortization to be equal with financial amortization, in practice economic entities establish the terms of economic use within the time span in which the normal functioning duration is comprised.

We can also mention that the term of economic use is an accounting estimation, thus, economic entities can modify it subsequent to the commissioning of that certain asset, fact that generates modifications of accounting amortization with all its implications upon the financial year's result.

The situation becomes more complicated if we also take into account the recoverable value of tangible assets at the end of the financial year when the impairment for non-current assets must be registered. Apparently, book value is objective, because at the moment the non-current assets are registered within the entity, it is validated on the market. One must not forget that in order to compare it with the recoverable value, from the book value one must subtract the registered amortization, the latter involving a series of variables.

Creative accounting techniques regarding the non-current assets' revaluation are usually used by the entities that suffer difficulties in order to increase its equity (revaluation reserves) and, thus, to artificially increase their debt capacity. Another place where creative accounting can emerge is the non-current assets production, by means of registering within the non-current assets' value the fixed costs (salaries and amortizations) related to the subtask.

In this sphere of creativity linked to non-current assets we can mention the lease-back operation which consists of selling a non-current asset to a leasing company, which is subsequently taken over in financial leasing. In this manner, the economic entity obtains the necessary economic resources in order to normally develop its activity and, at the same time, it can still use that certain asset, as if the entity still owned it. During the year the transaction is performed, the result increases, but it will decrease during the subsequent years by means of the leasing rates it will pay. The higher the transaction price is, the greater leasing rates and interests paid by the entity will be.

Concerning the financial assets the problem that raises is whether to include them in this category or within the short-term financial investments, thus, modifying the economic indicators and also the determination of adjustments for depreciation. According to the principle of prudence, every loss of assets' value must be acknowledged as an expense by determining adjustments for depreciation.

Another example is the one related to selling equity investments in a moment when the market report is significantly greater than the purchase price; afterwards, the entity proceeds to repurchase them. The same technique is used when updating the securities' input value and, simultaneously when increasing the result, even if the entity has to pay certain brokerage fees and the tax on the profit generated by the transaction.

Creative accounting techniques regarding current assets

Creative accounting regarding current assets occurs in the following directions: stock evaluation, volume of stored production, choosing the accounting method for construction contracts, the artificial cession of placement securities, the calculation and registration of adjustments for stock and receivable depreciation, etc.

The decision to constitute or not stocks of finished products enables an entity to improve its result.

The decision to continue the production, even without immediate usefulness, allows hiding the subtask costs and obtaining a favorable result. Certainly, there is the risk that the market will not accept these products without a firm order, and therefore, they will transform in loss in the next period.

The subtask's cost accounting can be another manner of creative accounting manifestation. In management accounting there are two manners of including fixed costs within products' costs: the full-costing method and the method of rational imputation. According to the full-costing method, the production cost consists of a share from the annual fixed costs in the following proportion: annual fixed costs x quantity in stock/annual produced quantity. According to the method of rational imputation, the production cost consists of a share fro the annual fixed costs in the following proportion: annual fixed costs x quantity in stock/annual normal quantity. In the first situation there is not such a subtask cost, all fixed costs being included within the production

cost even if the production capacities have not been used at their full capacity, while in the second situation the costs related to not using the production capacity is directly discounted upon the result without being included within the production cost.
Creative accounting can also manifest in what concerns the methods used (the direct method or inventory method, respectively the indirect method or accounting method) in order to evaluate unfinished production at the end of the financial year.
For the construction contracts which develop during a longer period of time one can apply two accounting methods: the method of progress percentage, when the revenues and expenses from the contract are acknowledged as the percentage of works in progress is registered within every financial year, which has as effect benefit distribution in every financial year; and the method at completed works, when the result is acknowledged only after the construction works are completed.
When using the method at completed works, the result will be acknowledged only at the completion of construction works, until then the value of registered expenses being acknowledged as work in progress.
In what concerns stocks, if their record is kept according to effective cost (purchase cost or production cost, as appropriate), the evaluation of stock outputs being made through FIFO, LIFO or CMP method, which, in case of inflation, ensure the achievement of different results. An entity's result does not only rely on real economic performances, but also on the option for a certain method of stock evaluation.
Another case of creative accounting emerges in the case of circular transactions, when two or more economic entities perform transactions amongst them in order to improve their results; for example, when two entities sell the same type of stocks at the same price to each another From the cash-flow point of view the impact is null, because everything one pays, one charges; from the VAT point of view the impact is also null because the purchase price is equal with the sale price. The sole difference is that the purchase cost of stocks would eventually increase (therefore, an increase of assets' value is registered) and, simultaneously, the result would also increase (the equity volume increases). In this situation, there is a price that the two entities have to pay in order to embellish their results, which is the tax on profit that registered an increase.
If the economic entities consider that there is a risk of not charging certain receivables, they can insure them. In this case there is no longer need to constitute an adjustment for receivables' depreciation. There are companies which, urged by the desire to achieve a good embellishment of the result, insure the receivables only after the depreciation is determined. Thus, if the company determines the depreciation in the first year and within this year it is registered a high profit level, it will be interested in creating an adjustment for depreciation. When the result is unsatisfying, it will insure the receivable, registering expenses with the insurance premium and revenues from adjustments (Malciu, 1999: 18-28). Creative accounting regarding short-term financial investments manifests by including them within the non-current assets category, by means of cessions of placement securities, followed by their repurchase when the sale price is significantly higher than the initial purchase cost, by registering or not adjustments for depreciation.

Creative accounting techniques regarding liability elements
Creative accounting regarding liability elements concerns share premiums which can be used in three directions: capitalization, including them within reserves and covering the expenses generated by new shares' issuance and sale. The expenses generated by issuing and selling new shares are initially registered as assets, within set-up costs and from this point creative accounting may emerge: either set-up costs are amortized and, therefore, the result is directly influenced, or set-up costs are covered by share premiums.

Choosing the second situation is justified by the fact that it does not affect any shareholder, but it favors the state by not including an expense within the result and, therefore, one pays a greater tax on profit. However, applying this situation, the result remains higher which misleads the external users who give priority to result variation and less to share premium variation. Another liability element taken into account are the provisions which have the role to cover risks, expenses or losses that are uncertain concerning their dimension or the moment of their emerging. They occupy an intermediary position between equity and debts. Because they require estimations, provisions create conditions for results' smoothing.

Another creative accounting technique is related to debts towards employees. This technique especially emerges within small entities where the associates are not limited to capital contribution, but they also make a work factor contribution. The remuneration for the work force is the salary, but in order to avoid pay taxes considered too high, the associates register themselves as self-employed persons which, according to their field of interest, pay an annual fixed tax, irrespective of obtained revenues. Therefore, in this case, there is a profit transfer within the entity which pays the tax on profit, by means of bills issued by entity's associates for their work, at the level of an individual who pays the flat tax. The associates win twice: firstly, they make savings from the tax on profit, and secondly, they do not have to pay the tax on dividends. This way, creative accounting is used for optimizing financial pressure, taking into account that the associates are not very interested in the information published within financial situations as the entity is a closed company (not quoted to stock market) of small dimensions.

A creative accounting technique that has a direct impact upon the result of the current financial year emerges within certain entities which establish by means of formal or informal agreements that the buyer may return the goods that have not been sold. Basically, this practice does not pursue to influence results but, in certain situations, it can be considered a method of result smoothing if in the year the sale was performed, economic performances are inappropriate. In this manner, in the year the sale was performed profit will be acknowledged, and the next year a decrease of profit will be registered in return.

One of the reasons for which annual financial situations are being approved after a certain period from the moment the financial year is closed is to identify events and transactions subsequent to that moment, but which actually belong to that certain closed financial year, in order to influence its results. If, at the end of the financial year goods sales are performed, followed by their return in the next financial year, which is previous to the approval of annual financial situations for the closed financial year, there are methods to remove the effects upon the result, as it follows: the revenues registered from sale will be annulled at the end of the financial year, and stocks will be considered as being produced by third parties and, therefore, stock variation related to sold products will also be annulled. The sole negative impact on the seller remains the VAT within the financial year in which the sale is performed, but it will be recovered in the next financial year.

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