

# **CREATIVE ACCOUNTING IN THE CONTEXT OF AN “EFFICIENT” MANAGEMENT**

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**Abstract:** This paper proposes an analysis of the creative accounting connection with the managing factor which administers informational resources in a company activity. Creative accounting, as it is defined in scientific literature, takes different shapes, “existential complexity” which makes it become the suitable environment of strategic and tactical steps, initiated and performed from the major objective point of view represented by the performance of the company. The manager is the one who connects the internal information, upon which he has control, with external information, in order to manage properly economic circumstances, the way of reporting financial results with influences on the perceptive of the company. An efficient management will follow the increase of financial indicators of the company and implicit of its performance, through financial insurance turnover necessary to the continuity and development of the activity of the company.

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## **1. INTRODUCTION**

The qualitative label “efficient” assigned to management, takes various forms of presentation based on subjective perspective in which it is appreciated. Thus, for shareholders, an efficient management is providing a benefit at least steadily, preferably growing, in the form of dividends. For employees, an efficient management is the one that provides an attractive package of social - professional and financial benefits. For collaborators (providers or beneficiaries), an efficient management is ensuring a level of equity in contractual relations, promoting the ones of “benefit-benefit” kind.

Connecting these benefits to the activity of a company, turns them into targets for managers, thing that creates pressure on the managerial act, becoming, depending on the individual judgment, stimulation that pushes the boundaries.

## **2. THEORETICAL AND PRACTICAL CONSIDERATIONS REGARDING CREATIVE ACCOUNTING IN THE CONTEXT OF AN “EFFICIENT” MANAGEMENT**

Although, from the beginning of the 90’s the theoretical basis of transparent management (open-book management) have been founded, established on the principle of accountability based on information and integration, the practice exposed introverted attitude only (close-book management). We believe that procedural opposite of the “utopia” open-book management is that according to which the users (of information)

should see just what they need to know. Thus, creative accounting becomes apparent, which in management context concerns those decisions that facilitate, regardless of underlying used tools, to achieve the objectives set by micro and macro economic situation.

Attracted in the economic sphere, goals turn into **results to be obtained** and integrated in scientific habits of creative accounting, “earnings management is the active manipulation of accounting results for the purpose of creative an altered impression of business performance.”<sup>1</sup>

Economic specialists who launched the concept of “creative accounting” are integrated within the term with a negative connotation, but in my opinion this connotation can be changed when there is an efficient management, which, using certain attributes of creative accounting can capitalize the entire activity of the company, including the creation of necessary liquidity.

Thus, replacing the verb “to manipulate” used by the authors C. Mulford and E. Comiskey with the verb “to provide” management results suggest the following definition of timeliness corresponding economic life:

***The management of the results represents the assembly of generation and presentation techniques of the of accounting results in order to promote an image of performant enterprise.***

What makes the difference is the development of strategies, depending on the impact of the results, conditioned by time dimension. Financial results generated only by traditional creative practice (under immediate benefits) does not create prerequisites for sustainable development.

For the purpose of supporting, by procedure, exhibited conviction that management in congruence with creative accounting practices can generate an appropriate development and application of the most effective strategies, we suggest the next conditionality cause and effect in the field of management sphere – “earnings management”.

Under strict conditional analysis highlighting the manipulative effects of creative accounting, C. Mulford and E. Comiskey researchers have identified that creative accounting techniques used by managers can ensure the premises to achieve the following advantages: ***increased market value of the company (share price effect), improvement of credit (borrowing cost effect), increase financial results (effect bonus plan), reduction of taxes (effect of legislative “loophole”***).

The cause of achieving these benefits, as it is supported by the researchers mentioned above, but can not generate lasting effects, so that point we present efficient ways of making, using strategies based on collaboration management with creative accounting practices, to achieve these.

**a. Increase of company's market value (share price effect)**

(The potential) investors are interested primarily in market stability and growth potential of the company. Through creative accounting techniques the results of financial reporting can be improved so that from the financial statements of the company, should result that this one can ensure continuous and sustainable income, and in conjunction with appropriate political activity, can materialize this flow in cash flow (oxygen, the catalyst of any activity).

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<sup>1</sup> Mulford, C. and Comiskey, E., **Financial Warnings**, New York: John Wiley&Sons, 1996, p. 360

One of the techniques by which management can ensure continuity and sustainability of revenue company image is the one called “raise money for rainy days”, that, even during less profitable, by making provisions established in years with very good financial results, as revenue can ensure consistency of positive financial results. I mention that not collecting provisions made for claims, guarantees to customers in years with good results, even if at the time of the constitution deplete their profit, representing as expenses at the time of collection they transform in recoverable revenue that the cash drawn-flow will allow the development company and thus maintain and increase the company's stock market value.

Another way that can harness existing cash flow resources is the offices of insurance companies for setting performance guarantees for the services to be provided by the company, for beneficiaries who ask for those guarantees having a high amount value. Thus, these amounts that would lock in guarantee deposits can be exploited in current turnover of the company and generate revenue and profit.

Another creative accounting technique is the timing for recovery or acquisition of assets. In this way, the increase of the market value of the company is ensured by investing a part of profit for creating technical facilities / performant equipment that makes a solid foundation for developing business activity in the medium or long term, even if the short term is a reducing returns to shareholders. In addition, addressing some of the profit reinvestment in assets to diversify activities is a technique related to efficient management combining diversification with sustainability.

In this context, investors will be willing to pay to “play” the same “game” as participants - shareholders whose wealth increases. By attracting investors, the company will have a “favourable feedback” - increasing the market value of the shares, reduce share volatility, reducing the cost of capital - immediately, with resounding impact in terms of image, other potential investors willing to pay higher prices.

#### **b. Improving credit conditions (effect of cost of borrowing)**

Credit institutions assess credit rating of the company, regardless of “contact” financial - contract or renegotiation. Depending on shareholder behavior, with appropriate influence evaluation indicators, the company can obtain favorable credit terms - relaxing financing contracts that act as a springboard to relaunch cash cost reduction due to the “dedicated” and reduce borrowing costs already incurred. In the case of contractual relations with credit institutions the same strategy can be checked.

In general, business performance evaluation criteria cover both the quantitative (outcome indicators) as well as qualitative (stability, continuity, development). Thus, it can provide creative accounting practices stability of income, but no match for the availability, the firm is not safe, something that may be offset only by an efficient management of creative opportunities.

Safer credit quality allows the company to be “courted” by appropriate offers adequated to the new “level of negotiation” obtained.

#### **c. Increasing financial results (effect of bonus plan)**

Creative accounting techniques exhibited many employees handling results due to the momentum of bonus plans.

The desire to increase accountability and individual involvement in increasing firm performance, some companies build schemes reward - motivation bonus in the form of X% of profit or opportunity to purchase shares “employee of the year” which received over X Euro, Y consecutive months, etcetera.

In this respect, employees are supported to use, in turn, various creative techniques for obtaining and reporting the desired result, except that sometimes they can generate fictitious increase of various indicators.

Efficient management will be able to mobilize employees in the desired direction by using effective communication techniques and by application of transactional analysis in the management.

Manager plays an important role through his consistently supported control on the employee's activity, whose dedication will generate a sustainable growth of the company. Therefore, we conclude that human capital work, although difficult to quantify the activity itself will certainly generate consistent financial results for the company.

#### **d. Reducing taxes (effect of legislative "loophole")**

Through creative accounting techniques can be shaped financial reporting measures, so to "meet" criteria "unfavorable" required by the legislation. Thus, for recovery in situations of recession, the state can provide a range of relaxing and supportive measures economic, fiscal, which will build effective management promptly.

In this respect, we mention some techniques that can turn over the view on financial results, such as:

- technique "raise money for rainy days" that I mentioned above will be used to reduce profit by increasing spending, creating reserves in the form of provisions for unpaid claims, guarantees to customers in the years in which financial results are supported by receipts to the invoices
- control technique by increasing revenue or expenses, using forms of accelerated depreciation of assets or opting for lower residual values at the acquisition of fixed assets
- technique "big bath" in which financial years with poor results, considered the sacrifice, is chosen for measures that increase costs, worsen or more, accounts, resulting in firm employment accessibility grid facilities tax.

### **3. CONCLUSIONS**

Effective management will use to develop the trainees tax benefit created by the activities which will be offset by all general tax items (assets, human capital and financial). As shown, the gross manifestations, creative accounting techniques only generate image benefits, intangible. Their inclusion in effective management practices will determine a set of levers which can act on material factors, human, financial impact in creating perceived benefits in terms of continuity and ensuring cash flow without which a firm cannot exploit its potential of photography.

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