Creative Accounting: A Literature Review

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Abstract—Our research objective is to show the effect of creative accounting on the performance of the company which uses these techniques to manipulate their accounts to show desired results. We also discussed about different types of creative accounting and parties involved in it and what are the motivation factors so that people are involved in creative accounting techniques. We also talked about Anglo-Saxon and European continental types of creative accounting in which they allowed different types of alternative method for creative accounting. We also analysed involvement of different professionals in creative accounting like accountant, lawyers and bankers. They help companies in deciding about the different instruments which help company to involve in creative accounting. Corporate governance can play an important role in financial reporting of the company because financial report shows the state of affairs of the company and investors take decision on the basis of financial report of the company. So it is necessary that financial report should show "True and Fair view' of the company. Professional and managers ethical responsibility is also discussed in our study. In which it is analysed who will be responsible for the failure of the company.

Keywords—Corporate Governance; Creative Accounting; Creative Disclosure Framework; Financial Reporting; Financial Scandals; Sarbanes-Oxley.

Abbreviations—Financial Reporting Standard (FRS); Generally Accepted Accounting Principles (GAAP); International Accounting Standard (IAS); International Accounting Standard Board (IASB); International Financial Reporting Standards (IFRS); Securities and Exchange Commission (SEC).

I. INTRODUCTION

WHEN we open this true Pandora's Box: Creative Accounting then we understands when and why exactly the concept first appeared and what influenced its development that arose many questions.

With hindsight a few favorable circumstances to this concept can be identified, circumstances first related to the economical advent of world states but at the same time to need of economic entities to create for them a good reputation in an increasingly competitive and tough economic environment. About this particular moment, that is first mention belongs to the founder of accounting Luca Paciolo. This ambition of making figure more appealing or opposite is as old as 500 years. Thus, Luca Paciolo was shaping in his already renowned De Arithmetica, the first accounting manual, practices of creative accounting.

Creative accounting refers to accounting practices that may or may not follow the letter of the rules of accounting standard practices but certainly deviate from those rules and regulations. It may be characterized by excessive complication and using innovative ways of characterizing income, assets and liabilities. Some times word like "innovative" or "aggressive" are also used for defining creative accounting. Creative accounting is a term which is used as a systematic misrepresentation of the true and fair income, liabilities and assets of corporations or organizations.

1.1. Definitions of Creative Accounting

Creative Accounting refers to the use of accounting knowledge to influence the reported figures, while remaining within the jurisdiction of accounting rules and laws, so that instead of showing the actual performance or position of the company, they reflect what the management wants to tell the stakeholders.

"Purposeful intervention in the external financial reporting process with the intent of obtaining some exclusive gain".

"Creative accounting is the transformation of financial accounting figures from what they actually are to what preparer desires by taking advantage of the existing rules and/or ignoring some or all of them" [Kamal Naser, 1992].

"Every company in the country is fiddling its profits. Every set of published accounts is based on books which have been gently cooked or completely roasted. The figures which are fed twice a year to the investing public have all been changed in order to protect the guilty. It is the biggest con trick since the Trojan horse. . . In fact this deception is all in perfectly good taste. It is totally legitimate. It is creative accounting" [Ian Griffiths, 1986].

'Is the deliberate dampening of fluctuations about "some level of earnings considered being normal for the firm"' [Barnea et al., 1976].

'Is any action on the part of management which affects reported income and which provides no true economic advantage to the organization and may in fact, in the long-term, be detrimental' [Merchant & Rockness, 1994].

'Involves the repetitive selection of accounting measurement or reporting rules in a particular pattern, the effect of which is to report a stream of income with a smaller variation from trend than would otherwise have appeared' [Copeland, 1968].

Schipper (1989) observes that 'creative accounting' can be equated with 'disclosure management', 'in the sense of a purposeful intervention in the financial reporting Process'.

Many terms can be used to describe the practices of changing the facts in accounting, e.g. cooking the books, aggressive accounting, massaging the numbers, window dressing, earnings management, etc.

Table 1: Common Labels for Financial Numbers Game

Label	Definition
Aggressive Accounting	A forceful and intentional choice and application of accounting principles done in an effort to achieve desired results, typically higher current earnings, whether the practices followed are in accordance with GAAP or not
Earnings management	The active manipulation of earnings toward a predetermined target, which may be set by management, a forecast made by analysts, or an amount that is consistent with a smoother, more sustainable earnings stream
Income Smoothing	A form of earnings management designed to remove peaks and valleys from a normal earnings series, including steps to reduce and "store" profits during good years for use during slower years
Fraudulent financial reporting	Intentional misstatements or omissions of amounts or disclosures in financial statements, done to deceive financial statement users, that are determined to be fraudulent by an administrative, civil, or criminal proceeding
Creative accounting practices	Any and all steps used to play the financial numbers game, including the aggressive choice and application of accounting principles, fraudulent financial reporting, and any steps taken toward earnings management or income smoothing
Source: The Financial Number Game by Charles W. Mulford & Eugene E. Comiskey, 2002 (John Wiley & Sons)	

II. Objectives

Objective of the study is to find out the relationship between creative accounting and types of industries which adopt creative accounting to manipulate the financial figures. Types of creative accounting mean how many ways creative accounting may be done and what are the solutions of creative accounting so that the effect of creative accounting may be minimized. Relationship between corporate governance and creative accounting. Ethical behavior of auditors to reduced the effects of creative accounting.

Who are the parties who will get the benefits of creative accounting and what is the after effect of creative accounting on the life of the organization. We have taken various examples of worldwide companies like Enron, WorldCom who have used creative accounting and shows different figures to compete with other companies and their after they collapsed.

We also try to look on the accounting standard parts which allow creative accounting and how it should be modified by the accounting authorities to reduce the effect of creative accounting because in present scenario, the accounting standards have some loopholes which provide alternative methods of accounting e.g. Recognition of revenue, methods charging for depreciation, recognition of cost etc.

What are the ethics and responsibility of an independent auditor and things to be keep in the mind at the time of auditing by auditors also looked in the study.

We are looking the answer of effect on financial reporting after making independent board in enterprise to reduce the impact of the creative accounting.

We also want to try the answer whether it is good or it brings company into the crisis. These are the some questions for which we want to search the answer.

III. Review of Literature

Hussey & Ong (1996) stated that creative accounting first became very prevalent in the 1980. Due to loopholes of accounting regulations, companies could produce accounts which flattered their financial performance. It talks about type of creative accounting like capitalizing interest, brand accounting, methods of depreciation, stock valuation, and accounting standards which prevent the major abuses which used to occur and has issued a number of regulations in the form of Financial Reporting Standards.

The main approaches which help accounting reader and prevent creative approaches by companies are:

FRS 1 Cash Flow Statements

Profit was easy to manipulate according to critics of creative accounting and therefore Accounting Standard Board therefore issued FRS 1 which requires most of the companies to publish cash flow statement. Although there are some technical problem with it.

FRS 2 Accounting for Subsidiary Undertakings

In the 1980's, there were a number of complex schemes where companies could bring profit without disclose their source of income and hide certain liabilities and assets from its balance sheet by operation of subsidiary style operations.

FRS 2 makes more transparent relationship between a holding company and its subsidiaries.

FRS 3 Reporting Financial Performance

This was a significant standard and has transformed the appearance of the profit and loss account, and also introduced some new financial statements. Instead of concentrating on single figure profit Accounting Standard Board considers companies to disclose information which reflects the various elements which make profit up.

FRS 4 Capital Instruments

This standard has the objective of ensuring that capital instruments are shown in financial statements in such a way that truly reflects the obligation of the issuer. Under this standard there was a clear definitions as to what must be shown as a debt, non-equity shares, and equity shares with clear rules.

FRS 5 Reporting the Substance of Transactions

In the past it has been possible for companies to report transactions in a way which has been legally correct, but has obscured the reality of the economic transaction. The standard attempts to rectify this by setting out definitions and the appropriate accounting treatments, particularly for transactions like consignment stocks, sale and repurchase agreements, and factoring of debts.

Naser (1992) stated that much is written about Creative accounting and about the various schemes of window dressing and off-balance sheet financing and very little information is available how widely such schemes are used by various companies. He has done a little empirical study to find the relationship whether creative accounting is related to the types of companies or industrial classifications, the reason behind the use of creative accounting, perceived legitimacy, consequences of the continued use of creative accounting, and measures to be taken to minimize its use. Because of much concern topic about creative accounting, it was difficult to obtain data from companies about their own creative accounting practices. However, it was felt by researchers that external auditors ought to represent an alternative source of creative accounting providing that their client information will keep secret.

In 1988, they sent copies of questionnaire to auditors and companies and got 15(out of 22) respondents that had had experience of auditing companies (7%) never encountered problem of creative accounting, 73% had found between 1 and 5 examples and 3(20%) had come across more than 5 examples. In this research he finds from his sample that private companies provided most frequents encountered examples of creative accounting and interesting was that all companies appears to make some use of it. Similarly for industrial classification, the result was that creative accounting was likely.

Uşurelu, Marin, Danailă & Loghin (2010) explained that the ethics in accounting and creativity. They stated that ethics should be followed by an accountant and creative accounting is big challenge for them. They talked about National Code of Ethics for Professional Accountants of Romania.

3.1. National Code of Ethics for Professional Accountants

It is divided into three parts. Part A establishing the fundamental of principles of professional ethics for professional accountants and also provide conceptual framework for applying these principles.

Part B and Part C illustrates how the conceptual framework should be applied in specific situations where Part A is not applicable code recognizes that accounting. Profession objectives are established to meet the highest levels of performance and meet the public interest.

Achieving these goals involves meeting four basic requirements:

- Credibility: Throughout society there is need for credibility in information and information systems.
- Professionalism: There is a need for customers, employers and other stakeholders can be clearly identified those accounting professionals.
- Service Quality: It requires ensuring that all services obtained from the professional accountant are carried to the highest standard of performance.
- Confidence: Professionals accountants' service users must be able to feel confident that there is a framework of professionals' ethics governing the provision of these activities.

Creative accounting is termed as synonym on for deceptive accounting.

According to him ethical behavior of a person in accounting depends on:

- Moral Sensitivity: Which could be described as how the subject comprehends the ethical dimensions of a situation. In accounting, one can feel that a practice can affects some people adversely or favorably. But there are also some sentiments of greed, self-sufficiency than those related to good behavior.
- Moral Judgment: Moral judgment or capacity to judge which alternatives are ethically acceptable and which are not. In accounting, objectivity, open mindedness insight and perspicacity can be considered as integrated within practical wisdom.
- Moral Motivation: Moral Motivation understood as willingness to take the moral course of action, placing moral values above the other values and taking personal responsibility for moral outcomes. It plays a crucial role in selecting the right action and in executing it.
- Moral virtues or permanent attitudes and interior strength formal behavior: among these virtues, those which have special relevance to accounting are truthfulness, honestly, loyalty, trustworthiness, fairness, integrity, service to the common good, gratitude and benevolence.

Courage, perseverance, competence, diligence, professional will help to defeat inner resistance to act as one should.

Practical wisdom has been said, provides capacity to perceive the right means for each virtue

Stolowy & Breton (2000) described that creative accounting is a concept dealt by professions particularly by journalist and academics to a lesser extent.

i. Creative Accounting in a professional perspective: creative accounting is an expression that has been mainly developed by practitioners and commentators (journalist) of the market. The motivation which they understood is what investors want to see, than what actually was to mislead them.
ii. Creative Accounting in an Academic Perspective: creative accounting also entered in academic literature, in the U.K. under the label of window dressing. Manipulations of such amplitude are hardy market anomaly. The behaviors of market participants are different than the efficient market hypothesis. The drama was that functional market hypothesis work better where manipulations was widely spread and have been dramatic effects on the understanding of risk and return potential of the firms.
iii. Creative Accounting and Creativity: creative accounting, as it is dealt with in a perspective, almost nothing to do with creativity. It is more likely to relate with accounting alternative than creativity.

However, there is on situation when accounting will have been "Creative". When a legal, economic or financial innovation occurs without any existing accounting standard to regulate it.

Smith (1998) classified accounting firms as "structured", "intermediate" or unstructured in terms of their audit methodologies. Using US data at a time when the Big 8 accounting firms still predominated, he classified 22 auditing firms. The number of accounting income increasing policy changes was higher for 'structured" auditors and massively lower for "unstructured" auditors.

Smith also reported on the accounting manipulations employed by 208 of the largest quoted UK companies and identified 12 different techniques in the common use, all of which would impact on the Profit and Loss account and Balance Sheet of the companies concerned.

The techniques specified can be described as follows:

1. Extra ordinal and exceptional items,
2. Pre-acquisition write down,
3. Deferred consideration on acquisition,
4. Disposals- profits on sales of asset taken "above the line" and deconsolidation of subsidiaries in anticipation of sale.
5. Brand Accounting- capitalization of assets,
6. Off-balance sheet finance,
7. Contingent liabilities,
8. Changes in depreciation policy(Method),
9. Capitalization of costs (interest and R&D),
10. Currency mismatching between borrowing and depositions,
11. Pension fund surplus used to reduce annual charge,
12. Convertible with premium put options or variable rate preferred stocks.

Out of above 12 techniques, those seven numbered as: 1, 2, 4, 8, 9, 10, and 11 having a cleared income effect.

Accounting policy change with an income effect is less clearly attributable to an auditor effect in U.K. study than his earlier Australian study.

Blake & Salas (1996) explained that creative accounting is seen as widespread in the U.K. and undermines the credibility as a disease.

During 1990's, creative accounting problem identified in Spain within the 'Continental European' model of accounted regulations.

There was an empirical work in Spain in which questionnaire was sent to 100 partners in Spanish audit firms. 29 replied, which was well above the average. They compared Spanish survey with two survey of U.K. on this topic with total 42 respondents. In both countries 30% of auditors consider creative accounting as legitimate business tool, while over 60% see creative accounting to be a serious problem. Where as in Spanish auditors, 28% think that creative accounting can not be solved completely and in U.K. 95% thinks so. They also compared Anglo American with continental European.

Matiş et al., (2012) described creative disclosure as a feature of creative accounting. It is also known as impression management in literature. It can be found in corporate annual report under forms of distortion of narratives of numerical and graph manipulation. They gave importance to theoretical framework than empirical study because interpretation of empirical analysis is impossible without theoretical guidance.

Creative presentation must be regarded as a complex mechanism that includes motives for engaging in manipulation of accounts, types of information disclosed and types of manipulation strictly connected to presentation of information.

There are two types of information disclosed:

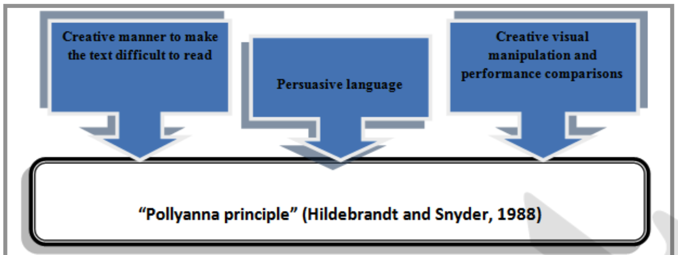
(i) Verbal information and
(ii) Numerical information

They are considered to be a part of following strategies which regard manipulations connected to presentation of financial information as follows the summarize form of strategies includes:

- Using a creative accounting manner to make the text difficult to read;
- Using persuasive language that comprises only positive words and emphasizes positive financial performance;
- Using creative accounting visual manipulation in the way information is presented with the scope of attracting the attention from other items that are important but in the same time are not flattering for the financial performance presented.
- Using performance comparison that involves choosing the benchmark that portrays current financial performance in the best possible light. They were explaining about the positive language used to report the financial information to stakeholders, which make them difficult to

understand the language used in reporting and they invest money in bad investment. This type of manipulation is known in the literature also under the name of "Positive Bias ".

- They also explained about "Polly Anna Principle" (concept introduced by Hildebrandt & Synder, 1988) managers used to present financial performance of the firm in the best light possible using only positive words.



Source: *Authors projection*

Figure 1: Creative Disclosure Framework

The creative visual manipulation disclosed information to influence decision, using creative visual effects to underline a part of the corporate report or an item in order to make it more oblivious to users (e.g. figures, font, style, size of the letters or numbers, color etc.)

To create a strong visual effect the ordering of the items location is also important like first part of the corporate reports can be chosen and those items which minimize the favorable direction last parts of corporate reports to be chosen.

As stated above information disclosed can be either verbal or numerical. The particular creative presentation is related to numerical which can be either inside numerical information the lowest prior, period comparative benchmark earnings number can be chosen to report in this respect the highest year-on-year increase in earnings.

In external numerical information can be constructed from the lowest competitors in a cross section analysis of industry performance.

Rabin (2005) described about auditors attitude towards creative accounting and ethical behavior of auditors. Auditor's ethical judgment is formed by the provisions of the code, organizational policies governing ethics and individuals own moral agency. Ethical judgment is fundamental to auditors in forming opinion whether financial statement fairly present the financial position, result of operations and cash flows of an entity and it is distinct from compliance with statements of GAAP Accruals are preferred method for manipulation accounting information because they are difficult to trace directly management can manipulate the timing of the reorganization of a transaction. The three dimensions of auditor's evaluation of the quality of financial reporting contained in the scenarios reporting practices (understandability, relevance and reliability) are:

Firstly, this finding seems to supports that quality assurance has come to be regarded as that the ethical principles section of the code has little impact on professional practice modeled in the formative mode.

This research article provides insights into the attitudes of auditors when they assess creative accounting practices and secondly, identified that relevance and reliability are more important than understandability in assessing the quality of financial information.

Thirdly, the findings of this study was that auditors perceive that meeting analysis and management targets, the maximization of remuneration and a lack of corporate governance are factors that influence the use of aggressive accounting by management.

However, auditor's attitude towards creative accounting were not associated with the existence of these factors and in the last point, research model find negative relationship between experience and auditors attitudes towards creative accounting, indicating that the more experienced an auditor is, the less likely it is that he/she will agree with management's creative accounting choices.

Cosmin (2010) described the various techniques used by the managers to get desired results.

A census (not exhaustive) of the techniques used in creative accounting:

1. Tangible assets: "subjective depreciation" of assets creates proper field of creative accounting of management estimates that recoverable value is lower than net accounting assets are considered impaired for difference. The result will be affected by recording a depreciation expenses.
2. Goodwill: Goodwill increases by underestimation of assets purchases capitalization and depreciation of goodwill during its useful life have influence on the outcome of further coming year.
3. Depreciation: Option for depreciation method has impact on the profit and loss during useful economic life of an asset. Thus, a different method of depreciation has different impact on outcome. An option on different useful life leads to different expenditure.
4. Inventories: The inventory provides sufficient opportunities of creative accounting and subjectivism. The under estimation or over estimation of stock finally has an impact not only on the financial statement of current year but also on the following year.
5. Provisions for liabilities and charges: A practice provision (increase and decrease thereof) is an effective tool for "leveling outcome". Establishment of provisions in those years where the profit results lead to decrease, while the resumption of the provisions in the income year in which the registers deficit increase leads to the result.
6. Construction contracts: Choosing between the two methods of accounting for construction contracts has the following impact on the profit and loss: - Under the completed contracts, the result will be recognized after the completion of contract, while in

method based on percentage of definitive result will be staggered over time, throughout the progress of the contract switching from one method to another method also impact on profit and loss account.

Mechanisms that have an impact on the balance sheet will be listed in the following table:

Table 2: Creative Accounting that Impact on the Balance Sheet

Elements	Mechanisms	Impact on balance sheet
Tangible assets	Lease-back: the sale of fixed assets, followed by taking them in the Immediate location.	- Improvement revolving fund; - Improve cash.
Tangible assets and equity	Revaluation of tangible Assets	- Increased asset value (increase in depreciation expenses) - Increased equity
Minority Interests	Inserting in equity, debt, or between the two alternatives.	- Change indebtedness and equity.
Loans	In substance defeasance arrangement by which the transferred assets to a trust, which incorporates the same time and management of debt.	- Reduced rate indebtedness; - Increase rate financial autonomy; - Increase financial profitability.
Customer Claims	Discounting of ticket Orders	Reducing the need for working capital; - Increased Treasury
	Assignment of claims from a pool of	Slight decrease of working capital (from the difference between price and value of transaction); - Decreased need for working capital - Increased Treasury

Source: Cosmin, L. I. (2010). A census of creative accounting techniques. Romanian economic business review, 5, 4-1 , 104-108.

Proposals on limiting the creative accounting techniques:

- First is the reducing the number of permitted accounting methods or specifying which method should be used in given circumstances,
- Trading links will be considered as a whole (substance over form),
- Encourage to regular review (revaluation of assets)
- Creating arbitration institution,
- Auditors should to intensify their efforts to identify the possible manipulation of information supplied by the financial statements.

Matis et al., (2009) explained taking Romanian example How cash is a king and Creative accounting impact profit and loss account and balance sheet but cannot impact on cash flow statement because it is a lot harder to manipulate because you can raise value or minimize value but you cannot make the money pops. So, it is not surprising that the scope for creative accounting is here quietly restricted but not impossible. In Romanian, managers have begun to look deeply into cash flow hedging opportunities techniques. As well as the creative accounting techniques, applied to cash flow reporting hedging techniques have an influence on future cash-flow, affecting the result in specific ways.

Cash flow hedging is focus on two main areas: Foreign Exchange and Interest risk management.

As far as foreign exchange hedging instruments and concerned the interest is increasing.

One of the simplest hedging instruments is a forward agreement, based on foreign exchange rate.

According it IAS 7, the amounts are to be included in cash flow report are actual amount paid or received. Therefore, the rates at settlement/payment data are used. The exchange difference is relevant in calculating the amounts paid or received. Unrealized foreign currency differences are not cash flows and will be excluded from cash flow statement.

In other area for cash flow hedging area is reserved for interest risk management. A simple and used method is IRS-Interest Rate Swap that has the effect foe the company of transforming a variable into a constant.

Based on fundamental research and both the discussion with experts in the field from Romania, we narrowed this vast area of creative accounting regarding cash flow at the following presented in Table 3:

Table 3: Creative Cash Flow Areas

Areas	Creative cash flow
Lack of honesty regarding accounts payable	A company has written a check for one of its suppliers and while the “check is in the mail” this particular cash manipulating company will not deduct the accounts payable with honesty and puts those amounts in the operating cash flow as cash on hand. Another way for a company to boost its cash flow image is related to delay in writing all their checks.
Non – operating cash	Non-operating cash is usually money which has nothing to do with business (e.g. money from securities trading). To include this particular non operating cash it would only distort the true cash flow performance of the company's business activities. They should be dealt with separately. The ultimate goal is to distort the operating cash flow.
Capitalization of expenses that are questionable	Not all of capitalizations of expenses are questionable. The capitalization became questionable if the expenses are regular production expenses, which are part of the operating cash flow performance of the company. If the regular operating expenses are capitalized, they are recorded not as regular production expenses but as negative cash flows from investment activities. While it is true that the total of these figures - operating cash flow and investing cash flow - remain the same, the operating cash flow boosted than that of companies that deducted their expenses in a timely fashion. Basically, companies engaging in this practice of capitalizing operating expenses are merely juggling an expense out of

	one column and into another for the purpose of being perceived as a company with strong core operating cash flow. The ultimate goal is to pop up the operating cash flow.
Selling Accounts Receivable	This is also called securitizing. The agency buying the accounts receivable pays the company a certain amount of money, and the company passes off to this agency the entitlement to receive the money that customers owe. The company therefore secures the cash from their outstanding receivables sooner than the customers pay for it. The time between sales and collection is shortened, but the company actually receives less money than if it had just waited for the customers to pay. So, it really doesn't make sense for the company to sell its receivables just to receive the cash a little sooner - unless it is having cash troubles, and has a reason to cover up a negative performance in the operating cash flow column. This can distort the operating cash flow from negative one to a much boosted one.

Source: Matis, D., Vladu, A. B., & Negrea, L. (2009). Cash-flow reporting between potential creative accounting techniques and hedging opportunities case study romania. Annales Universitatis Apulensis Series Oeconomica, 11(1), 140-153.

Elisabeta & Beattrice (2010) talking about agency theory in the field of creative accounting, which relates to the conflicts of interests between users of accountancy information.

An agency relationship comes into existence when one party, known as the principal, entrusts management of their assets to another party, known as agent, who has competence and knowledge inaccessible to the principal. The most common form of agency is that in which a manager operates on behalf or a shareholder.

From this point of view in the life of an enterprise. We can identify two categories of actors having a special position [Feleaga, 2006].

- On one side, the shareholders, who have rights after the creditors, suppliers, employees etc. they take the financial risk justifying the appropriation on a part of the year’s profit and from the case of the entity closing down,
- On the other side, the leaders because they have privileged information, taking into account the position held in the enterprise and, therefore are tempted to take advantage by allowing themselves considerable advantages or generally by, directing the entity towards a direction which is useful for them.

The conflict of interest among different interest group is the real cause of creative accounting. Managing shareholders interest is to pay less tax and dividends. Investor-shareholder wants to get more dividend and capital gains. Country’s tax authorities like to collect more and more taxes. Employees want to get better salary and higher share in profit. But creative accounting puts one group or two groups to advantageous position at the expense of others.

The IASCs framework for preparation and financial statement, envisaged by the IASB. Presents the following categories of users: current on potential investors, employees, creditors, suppliers and other commercial creditors, client, government and governmental institutions and the general public. They may be divided into internal and external users.

Internal users are principally management personnel within the company. They have responsibility to release information and external users come into other categories.

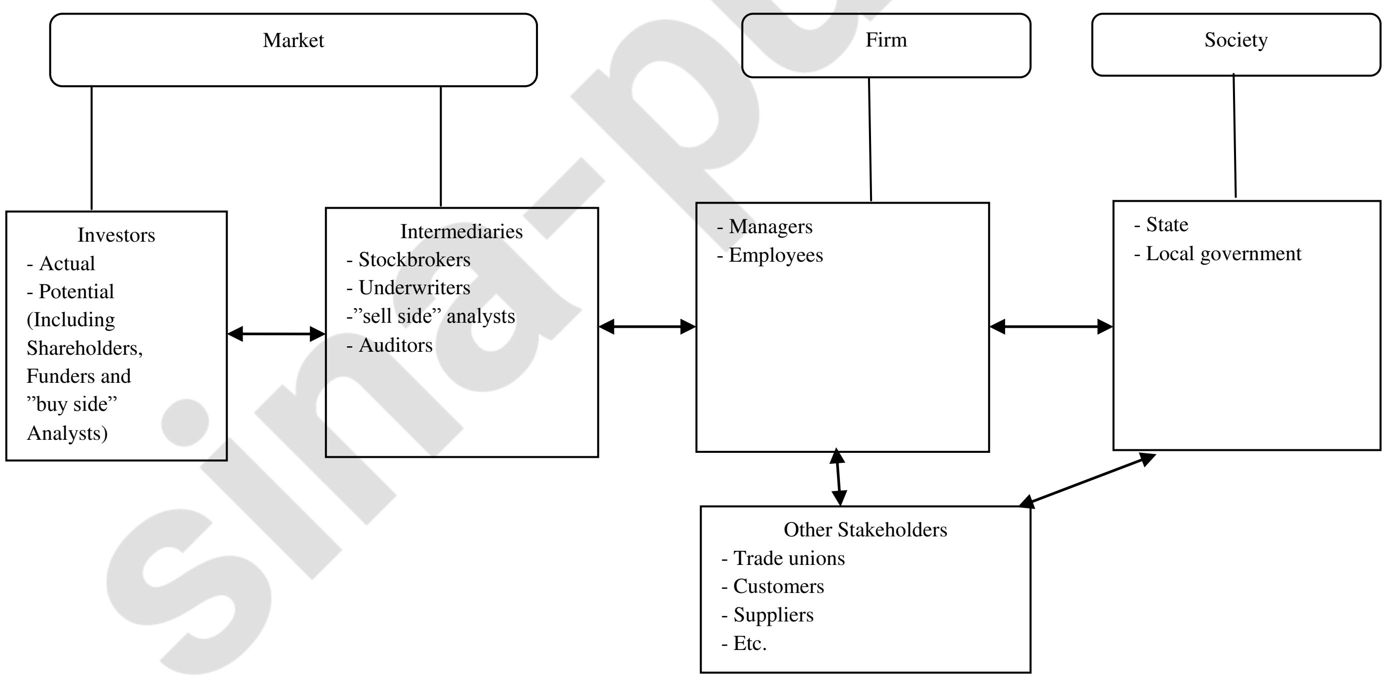


Figure 2: Players in the Field of Accounts Manipulation

Source: Stolowy, H., & Breton, G. (2004). Accounts Manipulation: A Literature Review and Proposed. Review of Accounting and Finance, 5-92

The investors can be divided into four sub-groups: real and potential shareholders and the real and potential stakeholders.

Managers may or may not believe in market efficiency. In case they do not, they can under to manipulate the number to reduce the cost of capital and to satisfy demand of external existing shareholders, to increase their own remuneration, to decrease the overall risk of firm, or to avoid violating the debt covenant or incurring political capital costs.

Table 4: Potential Gains and Losses in/from Manipulating Accounts

Players	Gains	Losses
Managers	Reducing the cost of capital Keeping their job Managing their remuneration Respect the debts covenants Official examination Minimization of income tax Gain tax advantages Improve relations with creditors, employees and investors Avoid political costs	The job and reputation
Existing shareholders	Increase the market value of their bonds Controlling employees claims	Wealth transfer to the actual Shareholders
Existing bondholders	Increase the market value of their bonds Controlling employees claims	Wealth transfer to the actual Shareholders
Employees	Keeping their jobs Increase the remuneration	Their job from an unexpected Bankruptcy
Suppliers	Keeping their client	Some money following an unexpected bankruptcy
Clients	Continuous services Warranty respected	Services interrupted Warranties not honored
State	Tax to collect Jobs for people	No more tax to collect Unemployed people to provide for
Bankers	Repayment of the loan	Some money following an unexpected bankruptcy
Society	Keeping the job Production of wealth	Jobs lost and resources wasted

Source: Stolowy, H., & Breton, G. (2004). Accounts Manipulation: A Literature Review and Proposed. Review of Accounting and Finance, 5-92

Shah et al., (2011) tried to give answer that why do managers do creative accounting and how they become successful in performing such practices in the presence of stringent rules and procedures. They also tried to explore whether creative accounting practice is good or bring crisis in the companies and link of corporate governance with creative accounting. Many world examples given like Enron which show higher profit than actual and then collapse. The role of debit and credit has also explained in which playing with different items like assets, expenses or liabilities which creates creative accounting and increase or decrease profits according to their wants.

Corporate governance can play role to reduce the risks of investors and show true and fair view of financial reporting. There are some choices in current accounting rules under International accounting standards and U.S. GAAP that allow managers some choice in determining methods of measurement and criteria for recognition of various financial reporting elements.

Financial report should be audited by an independent to reduce the information risk and to enhance perceived integrity.

The audit committee of the board comprising of independent non-executive role to prevent misuse of creative accounting techniques and observance of ethical standards in financial reporting. It was explained that it is not that creative accounting solutions are always wrong. It is the intent and the magnitude of the disclosure which determines its true nature and justification.

Table 5: Rewards of the Managing Profits (Earnings Management) & Financial Position

Category	The Objectives & Benefits Companies Trying To Achieve
Share-Price Effect	Higher Share Price Reduce Share Price Volatility Increase Firm Value Lower Cost of Equity Capital Increased Value of Stock Options
Borrowing Cost Effects	Improve Credit Rating Lower Borrowing Costs Relaxed or Less Stringent Financial Covenants
Management Performance Evaluation Effects	Increased Bonuses based on Profits/ Share Price
Political Cost Effects	Decreased Regulations Avoidance of Higher Taxes

Source: The Financial Number Game by Charles W. Mulford & Eugene E. Comiskey, 2002 (John Wiley & Sons)

Fišerová has explained creative accounting in context of joint stock company that how they show fiction statement than reality to take a loan they show higher value of assets, low profit again at the time of paying tax to the government and again profit increases at the end of the year when information is to be given to shareholders.

Creativity in the accounting comes at a time when it should reach to the public in the form of true background, figures and results. This transforms the actual financial statements to those which the owner would like to achieve as positive and favorable results of the company. It is the shareholder and director who are responsible for the accuracy of accounts. But the paradox remains with the fact that the expert must to find out the accounting and tax levers to fix situation when the enterprise gets into trouble through its creativity. It was also explained that whatever reason whatever is creative accounting will always be reflected in financial indicators and ultimately at the company solvency, because not everything which looks like a profit is really a profit. The truth is even that at the moment of artificially overestimation of financial ratios of the company could fall into solvency, bankruptcy, insolvency etc.

Creative accounting could be restricted at so-called harmonization of financial reporting and by application of mandatory IFRS (International Financial Reporting Standards) IAS, which are international guidelines for accounting also preparation and presentation of financial statement published by the International Accounting Standard Board (IASB).

Teodora & Nicolae (2009) has taken 110 samples to explain the level in which financial accounting professional comply with the professional ethics standards.

Based on results of survey they found managers do not agree with the statement that "financial-accounting innovation and creativity" is fraud. In their first hypothesis testing questioned and they found based on survey results that the financial accounting creativity and innovation is a well-appreciated performance. Survey results are also explaining why creativity and innovation is used by companies and they found the answers by their survey was that they want to get additional financial resources, the desire to avoid legislative ambiguities and tried to explain answer why companies do not use creativity and innovation was-

Correctness, fear, existence and internal and financial auditors, stakeholders.

Anonymous (1997) has explained what are the economic incentives of creative accounting. Choice of creative accounting is not causes because of performance but the specific characteristics of the company. The relevant economic variable gearing, size and earning volatility are measurable and give predictable results. As more as a geared a company the greater its use of creative policies to increase its reported earnings. Larger organisation and those in monopolistic, or more regulated, industries also have an economic incentives to employ creative accounting. Companies with economic power because of their bigger market size tend to reduced or smoothed profit to avoid the attention of monopoly authorities or costly lobbying by other groups with a political agenda. Companies in the water industries, hotels and leisure and brewing employ more creative accounting techniques than companies in the electricity and financial service industry which employ fewer.

Company's auditor also play a role to determine the extent of creative accounting use in the company. Research done and found that in big firms also auditors allow creativity. The link between variables such as gearing, size and earnings volatility and accounting policy choices occurs because imperfection in capital markets create a real incentives for companies to adopt creative accounting.

Park (1958) kept different approaches to explain the types of thought necessary for developing accounting idea's principle. What are the thought process in creative accounting and how we organise our thinking.

Creative thinking is necessary for measuring enterprise financial position and operating performance and providing information geared to managerial decision making. Mere technical advancement cannot fill the bill. The impetus for creative development must come in greater measure from thinking generated within the intellectual circle of our own profession. Must create receptiveness for the innovations and should anticipate the demand for each new informational device and its supporting rationale and educate the users of financial information to their future needs

Nurturing open minded attitude need creative accountancy research in accountancy. Office and factory are laboratory of accountant. The general theory and technique of accountancy will achieve its brillion future through directed creative effort.

To accomplishment of objectives stated above involves applying scientific method, eliminating logical fallacies and using operational approaches to creativity to solve accountancies problem and for expanding perimeter of its theory.

Moldovan et al., (2010) focused on how information provided by accounting effects external users, and mainly on how and why distorted information gets outside of the organisation into the hands of unsuspecting users. It was also explained there is a inverse casual relationship between true and fair view principal and creative accounting.

"True" and "Fair" cannot be defined easily. Definition given by some authors to this concept, first "true" and "fair", nether of which are easy to define and secondly there are those who explain true and fair view in terms of " generally accepted accounting principles rather than accepting the concept as an independent quality".

True and fair view through financial report's respect both word of law and its spirit. It is acknowledge that true and fair view expresses the responsibility of company management and auditors to show the correct financial position of the company.

In the anglo-sexon accounting system this principle is valued more than any principles. As using more set of accounting policies overriding for true and fair view which provides accounting choices for different methods. The chances of creative accounting increases. But it depends on intention. If intention is not bad it will give true and fair view of accounting information.

3.2. Professional Ethics in Creative Accounting

Creative accounting is a challenge for the accounting profession. In practice, the situation in which under the pressures of the management, the accounting professional applies a certain accounting treatment provided by the laws and regulations which show different image of the organisation than true and fair one, which are countless. The accounting professional is forced to balance ethics, accounting principles and their job.

It also tries to answer whether creative accounting is fraud? But it said creative accounting technique can be called aggressive accounting but it is not a fraud because it is not against the law.

A poor corporate governance is leading factor together with a weak internal control and a lack of honesty and transparency in presenting the company's performance which allows creative accounting to crawl in.

For the solution of creative accounting cash flow statement is suggested because it is not easy to manipulate accounting in cash flow than accural base system. Forensic accounting should be taught to the students to know the dangers of getting involved and how to detect the application of such techniques.

Gherai & Balaciu (2011) has taken examples of accounting scandals that have left traces in the history due to their strong impact like the Enron phenomenon, Paramalat, Worldcom, Xerox, Xerox, Ahold Royal, or Equitable Life bankruptcy are few examples.

Enron, WorldCom which were collapsed in year 2002 used accounting techniques to show manipulated accounts which decrease the confidence in financial reporting, audit reports and regulations governing the professional accountancy. To improve old rules and setup new stream lines were supported by all countries effected by the bankruptcy crisis.

Thus the law Sarbanes-Oxley from 2002 is one of the reforms that have repercussions throughout the world by adopting the standards belonging to foreign trade companies in U.S. market and determination of other countries to study its provisions and act on his own benefit. Many countries made law related to corporate governance like New Zealand and Australia.

Companies show different depreciation method, life of assets, residual value of assets to fluctuate the earnings. Mangers have role to shows fluctuating profits which puts firms into financial crisis after showing profits and growth in beginning year then they collapsed. To exclude creative accounting from balance sheet auditors and management have to play a big role and provide true & fair view by financial reporting. It is not possible to eliminate creative accounting completely.

Vladu & Matiş (2010) tried to explain the topic of creative accounting and corporate governance in the context of internal demand for manipulative behavior which emanates from the contracting value of earning management in the principal-agent relationship between shareholders and mangers poor corporate governance causes manipulating accounting practices.

The topic of information asymmetry is also discussed since no approaching regarding creative accounting omits it. In which one party has better information than other party in the context of managers and shareholders where manager has more information than shareholders in an enterprise. Information asymmetry work in context of capital market. The CFO and board of company know more than the shareholders and other users about the profitability of the company.

Five theories have provided the theoretical underpinning for research opportunistic behavior in the area of corporate governance.

Which are:

- Agency theory
- Legitimacy theory
- Institutional theory
- Signaling theory and
- Stake holder theory

Describing different aspect in association with managerial opportunistic behavior.

There are two different patterns through which companies are financed and both of them affecting accounting earning the companies are related to the corporate governance model that prevails in a particular country. If corporate governance model is the shareholder model if countries belongs to the Anglo-American accounting model. Capital market has a great role in financing companies in the context and as consequences great importance will be put on information available to share holders. Companies are dominated by equity shares and there is a great separation between managers and owners and as consequences information exists and incentives to manipulate accounting information are considered to be strong.

If a country belonging to euro-continental accounting model, then the corporate governance model that is reflected in this context is the stakeholder model and great emphasis is placed on the information presented to the creditors (e.g. Banks).

Five basic subjects are covered by the OECD Principles of Corporate Governance as following:

- Protection of the rights of shareholders;
- Equitable treatment of all shareholders comprising full disclosure of material information and also the prohibition of abusive self-dealing and insider trading;
- Equitable treatment of all stakeholders as established by law and encouragement of cooperation between company and stakeholders;
- Timely and accurate disclosure and transparency with respect to matters material to company performance, ownership and governance;
- Strategic guidance of the company and effective monitoring of its management by the board of directors as well as the board's accountability to the company and its shareholders ensured by the corporate governance framework.

Healy & Wahlen (1999) described about how standard setters should decide or make accounting standards to reduce the possibility of earning management. Information about the company is provided by the financial reporting which should show the true and fair view of company but managers manipulate the financial numbers than actual due to their personnel interest like to increase their management compensation, to provide low salary to employees, to pay less dividends to the shareholders.

Standard add value if they enable financial statement to show difference between the relevances and reliability of accounting information under alternative standards.

The chairman of SEC, Arthur Levitt, express worried over earning management and its impact on resource allocation. Some creative accounting techniques noticed like pre-mature revenue recognisation, cookies jar reserves, and write-offs of purchased in-process R&D are threatening the credibility of financial reporting. In this article, reviewers want to find the answer of a central question for standard setters and regulators, therefore, is to decide how much judgement to allow management to exercise in financial reporting.

The standard setters are likely to be interested in evidence on:

a. The magnitude and frequency of any earning management,
b. Specific accruals and accounting method used to manage earnings,
c. Motives for earning management and
d. Any resource allocation effects in the economy.

Much of the academic research on earning management is of only limited value to standard setters and regulations.

Earning management occurs due to various reasons, including influence market perception, to increase management compensation, to reduce the likelihood of violating lending agreements and to avoid regulations.

Balaciu et al., (2009) has done short review of creative accounting topics and its development to know about what are the motivations for creative accounting literature and solution to this creative accounting term. They tried to correlate creative accounting with different interest area like bankruptcies, audit, governance, financial market, the public sector and quality of financial reporting to prevent creative accounting by taking various articles from scientific data source like Science Direct, Emerald, Repec, Google Scholar etc.

Amat et al., (1999) perceived the various methods of creative accounting can be considered to fall in four categories:

i. There are different options to choose accounting methods sometimes like in many countries for example; a company is allowed to choose between a policy of writing off Research and Development expenditure as it occurs and amortizing it over the life of the related project. A company can therefore choose that accounting will give them preferred image.
ii. Some entries in accounting involve an unavoidable degree of estimation, judgment and prediction. In some cases for example, in estimating life of an asset for calculating depreciation, these estimates are normally made inside the business and the creative accountant has opportunity to err on the side of caution or optimum in deciding estimate.
iii. Artificial transactions can be entered for the purpose of manipulate balance sheets amount and increase profits between accounting periods, which is achieved by two or more related transactions with an obliging third party, normally a bank.
iv. Genuine transactions can also be timed so as to give the desired impressions in accounts.

Following are the methods which can be used to tackle each of these approaches by accounting regulations who wish to curb creative accounting:

i. Choice of accounting methods can be reduced by reducing the number of permitted accounting methods or by specifying the circumstances in which each method can be used.
ii. Abuse of judgment can be curbed in two ways. One is to draft the rules that minimize the use of judgment and second is apply 'consistency' so that if one country applies one method which suits in one year also applies the same in unfavorable year.
iii. Artificial transactions can be tackled by invoking the concept of 'substance over form where by accounting substance determines by economic substance rather than legal form of transactions.
iv. The timing of genuine transactions is clearly a matter for the discreation of management. However, the scope to use this can be limited by requiring regular regulations of items in the accounts so that gains or losses on value changes are identified in the accounts each year as they occur, rather than only appearing in total in the year that a disposal occurs

3.3. Reasons for Creative Accounting

Following are the reasons for the directors of listed companies to manipulate the accountants are as follows:

- Income Smoothing, company prefers to show steady growth in profit rather than fluctuating high or low. So, companies charged provision for liabilities against assets to reduce profits in good year.
- A variant on income smoothing is to manipulate profit to tie in to forecasts.
- Company directors may keep an income –boosting alternative in hand to avoid unfavorable news.
- Creative accounting may help maintain or boost the share price both by reducing the apparent levels of borrowing, so making the company appear subject to less risk by creating the appearance of a good profit trend. This helps the company to raise capital from new share issues, offer their own shares in takeover bids, and resist takeover by other company.
- Manager can use creative accounting to delay release of information for the market, thereby release of information for the market, thereby enhancing their opportunity to benefit from inside knowledge if the directors engage in 'insider dealing' in their company.

The position taken by Ruland (1984) and compare it to Revsine's analysis on following notes:

- Moral rules apply to actual action and the teleological view that an action should be judged on the basis of the moral worth of the outcome.
- Positive responsibility, which here would be the duty to present a 'negative' and 'unbiased' accounts where managers are responsible for state of affairs they fail to prevent.
- 'Duty to refrain' would imply avoiding the bias inherent in creative accounting while the 'duty to act' would involve pursuing the consequences to be achieved by creative accounting. There had been many ethical surveys done in Spain and U.K. to decide about the ethical value of accountant which showed Spain thinks creative accounting less dangerous than U.K

Shah (1996) examined the process of creative compliance in case of complex convertible securities issued by U.K. listed companies between years 1987-1990. There was an active dialectic of creativity in designing these types of instruments. A thift from avoidance to rules to avoidance again.

Lawyers, accountants and bankers all were involved in creative compliance.

During 1987-1990 convertible securities attracted a lot attention from financial engineers. At that time there was no laws or standards of accounting for the treatment of convertibles so, no rule stated whether it is taken as equity outset or coupon rate is charged to profit and loss account. It was this gap in rules which provided creative accounting. Than again one more such instrument premium convertible bond comes into existence. One of the difficulties of analysing the process of creative compliance is the potential sensitivity of data collection as one of the most obvious sources of evidence.

It exposed closed co-operation between various groups of professionals-lawyers, accountants and bankers- in the development of the scheme. Companies were willing to subscribe this scheme at significant cost and for a while, successful creative compliance was attained, regulators were slow to respond and when they did make pronouncement, companies once again circumvarented the rules with the help of various professionals. Auditors compromised their positions as quasi-regulators and permitted companies to circumvent best practice. Close exposure also exposed the involvement of lawyers in the designing of these instruments, suggesting that creative compliance schemes requires direct co-operation from professionals who are familiar with the existing regulations and can provide the necessary credibility to the new schemes. Small groups of professionals were also involved in designing and execution of scheme perceived commercial benefits that they went on market them to new potential clients with the hope of enhancing their profits.

IV. CONCLUSION

After reviewing different articles from different scientific data source like Science Direct, Google scholar, Jstore and Emerald etc we can say that creative accounting is biggest problem in showing financial reporting disclosed by the companies which is affected by different incentives perceived by the different interest groups in the company like mangers want to show higher profit to increase their compensation, to increase market price of share of the company and show low profit so that they can deny the demand of increase in salaries and incentives of the worker and have to pay low taxes to the government.

Creative accounting is not a fraud but it takes the benefits of loopholes in the accounting standards and regulations. It cannot be said fraud because it works within the framework of law. It takes advantage of multiple options available in accounting standard to show the transactions like different methods of depreciation method and estimating useful life of the assets, different options available in revenue recognition as well as loss recognition, different methods are available in valuing stock inventory whether use lifo or fifo method for valuation of inventory. Managers use that method which increases their benefits in that year and shows higher profit.

V. RECOMMENDATION

For improving financial reporting quality and to increase the faith of investors in company's financial report corporate governance can play a big role in which independent directors can be chosen by the shareholders which works upon the mangers activities and keep eyes on managers activities. Because financial reporting is true indicators company's operating activities and should provide true information to shareholders about the company's state of affairs. So that investors can take decision to invest in company or not. In that area, independent auditors can be employed to check the state of affairs of the company and give true and quality information to the share holders and stakeholders like creditors bank etc. they should work without any pressure of the management.

Ethics of auditors is also explained in which it was discussed that auditors have some ethics to the society and mangers have also some ethics to not show the manipulated figures but to show true and fair view of the company. Mangers should take responsibility of bad position of the company. Auditors should provide good information to shareholders and check all the transactions and can ask from the managers any suspicious account or dubious transactions. They should provide quality and competent service to their customers. An auditor should be confident, good knowledge of existing law and regulations and he should be updated.

In the solution part of the creative accounting regularities body should make law which reduces the chances of alternative accounting methods. They should make the provisions of that if one company chose one method in good year it should choose same method in unfavorable year also.

In the end we can say that it is not possible to reduce the impact of creative accounting completely because of involvement of mangers and auditors and slow work of regularities bodies. We can work towards to reduce the impact of creative accounting to some extent by credible accounting in which it is to be stated that the impact of creative and fraudulent accounting can be reduced by streamlining the accounting and auditing system and more effective corporate governance.

In India creative and fraudulent accounting can be reduced by:

- Introducing forensic accounting for white collar fraud detection and fraud prevention;
- Reducing the alternative choices of accounting treatment in accounting standards;
- Enhancing the quality of corporate governance;
- Amending Companies Act;
- Enforcing strong regulation, and
- Increasing the effectiveness of audit.

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