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CREATIVE ACCOUNTING PRACTICE: DOES IT COMPROMISE THE INTERGRITY OF ACCOUNTING ETHICS

Bachelor's thesis

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I declare that I have complied this thesis independently.

All works and major viewpoints of the author, data from other sources of literature and elsewhere used for writing this paper have been referenced.

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ABSTRACT

The primary purpose of this paper is to explore the ethical behaviour behind of creative accounting and how is perceived by management, accountants, users and potential users of financial statements.

Almost all financial statements are used by internal and external investors to determine whether is profitable or not to invest in a company. Banks and other financial institutes also depend on the financial statements to ensure companies have a proper cash flow management and adequate credit when determining to give loans. With all of these extra eyes monitoring a company's financials, along with other factors which may come into play, managers have started to manipulate the numbers on their financial statements to show higher numbers than actual, to give their companies a good impression from the outside and even internally to ensure their position at the top is secured. Thus, the issue of creative accounting.

In this paper, the author seeks to view the practice of creative accounting from an ethical accounting point of view. Where the concept comes from, is it a perception of a person, how the idea is perceived and is it to determine whether the standards can be manipulated for original account, and if yes what drives them. The author finds this to be a fascinating topic which has become a common practice for businesses in accounting and sets out to determine the ethics, the methods in which the manipulations can be done and whether or not this practice can be controlled.

Keywords: accounting, creative accounting, financial statements

TABLE OF ABBREVIATIONS

IFRS	International Financial Reporting Standards
GAAP	Generally Accepted Accounting Principles
IASB	The International Accounting Standard Board
CA	Creative Accounting
COGS	Cost of Goods Sold
IPO	Initial Public Offering
IASC	International Accounting Standards Committee
ISA	International Accounting Standards

INTRODUCTION

The encompassing goal of this research is to explore the ethics and impact of creative accounting, how it is done and how financial statements are manipulated through creative accounting. I will also explore measures in which creative accounting can be managed or be reduced, to present more factual information for those who need it.

Accounting can be treated as art on an account that it calls for original judgement and skills. To be able to carry out accounting functions efficiently, education and guidance are required. Accounting is also known to be a science due to the reasoning that it is a body of knowledge, but it is not considered a rigorous science because the rules and principles of accounting are regularly changing and developing for the better. (Sokanu, s.a)

Fabrications and changes have many ways to be attained and may be due as the result of various reasons. This practice can be leading to a considerable influence on the earnings reported by companies at the end of the financial period.

Financial Statements are the instruments through which investors, stakeholders attain knowledge about the economic situation and functioning efficiency of a corporation. The truthfulness and dependability of these financial statements are essential for all parties who are investing or currently hold stakes within or company or even potentially becoming one of those individuals to be able to make the most suitable decision.

Creative accounting is a practice that is a part of a game called the financial numbers game. It is one of the primary labels of the financial numbers game. The other names are Aggressive accounting, Earnings management, Income smoothing and Fraudulent financial reporting (Mulford & Comiskey, 2002). The main characteristic is to modify the financial statements to give a misleading impression of a firm's performance. When information on creative accounting was first published it was quoted in this way, "Every company in the country is fiddling its profits, almost every set of accounts is based on books which have been gently cooked or completely manipulated." (Jones M. J., 2015)

Although most would not admit to this practice, managers across the globe are using creative accounting to their favour to outplay investors.

The international accounting standards committee (IASC) was started in 1973, with the primary goal to standardise international financial reporting, the IASC developed and published international accounting standards and further encouraged their worldwide recognition and acknowledgement. Initially, the measurements of the model formed by the IASC contributes to allowing alternative means of measuring or publishing financial information. An agreement was done on the act of one's own free will, and so allowing more than one satisfactory or agreeable way of handling a particular accounting issue was a way to guarantee support for the standard. The central effect was then the restriction of the more unacceptable or what may be seen as unethical practices instead of the primary purpose of attaining a collective agreement and relation. (Pendlebury & Groves, 2004)

Even though accounting standards are provided, it still leaves space for various types of loopholes. The International Accounting Standard Board (IASB) and the Financial Accounting Standard Board (FASB) are both accounting foundations which provides the groundwork for the preparation and development of accounting standards. The reason for having this framework is so that the users of financial statements comprehend the practices and standards which are based on one accepted view. The rules also implement direction or instructions for unusual transactions, which may differently be subjected to perception. (Pete, 2018). The information presented in the firms is for the most part intended for the primary users, which are usually made up of high-risk investors. Therefore, these principles or rules should assist these high-risk investors, who are the primary source of risk capital to the firms. These standards should ensure that the data they are presented with will be of aid to them, by accomplishing superior decisions and not only for the enhancement of the business so that it can achieve a higher capital. (Sakkal & Nadim, s.a)
This bachelor's thesis focuses on qualitative research, of accounting professionals, managers, current and potential users of financial statements from around the world. The purpose of this work is because for the past two decades in the accounting professional and business environment there exists a growing issue of ethical scandals among large establishments and accounting firms. The option to choose between what is ethically right and personal gains is a widespread issue that needs to be explored to curb unethical practices.

Lastly, I would like to acknowledge and thank my supervisor Vaiva Kiaupaite-Grushniene for here time and assistance. Without her guidance and feedback this paper would have been more difficult to complete. To complete this thesis required more than the support of my supervisor, acknowledgement goes out to my colleagues at Tallinn University of Technology, in times of support and motivation we were there for each other, also much thanks to the librarians at TTU for their assistance in finding books which were used in this paper and also to TTU library for providing the database which allowed us to assess to the information and data I needed. And finally, thanks to God for the strength, knowledge and guidance when asked upon to assist me in pushing through and completing this paper.

1. THEORETICAL BACKGROUND OF ACCOUNTING

1.1 Conceptual Framework of Accounting Ethics

An excerpt from (Bean & Bernardi, 2005) states, "Dishonest activities at Enron, WorldCom, HealthSouth, and other companies have had destructive effects on the financial markets and investors. When upper management plays with the numbers, the public often assumes that the accountants and auditors act as willing and active participants in the process."

Accountants are liable for reporting accurate data about an organisation. Being an auditor there is an obligation to reevaluate financial statements, to verify that the information presented is reliable and trustworthy. The accounting occupation has constructed various codes of ethics which decides the systems for an accountant's conduct. The codes demand the need to comply with the law to the fullest extent. These rules dictated what is expected and required of an accountant ethically. (Duska, Duska, & Ragatz, 2011). So, order for the profession to not lack the credibility and morale of those who rely on it.

"The U.S had a code of professional ethics for CPAs that relies upon the rigorous independence of auditors from their clients. The need to approach an audit with a healthy dose of scepticism and a scientific mindset; and an integrity standard that requires CPAs to not give in to the pressure of a superior or client to deviate from proper accounting and financial disclosure standards. Top management may want their financial statements to "tell the clients' side of the story" rather than present financial information by GAAP." (Mintz, 2010)

The International Federation of Accountants IFAC mission is to serve the public’s best interest by observing and complying with the ethical requirements. The fundamental principles are listed in the table below.

Table1: Professional, the general application of accounting code of ethics.

Integrity	110.1 A professional accountant should be straightforward and honest in all professional and business relationships. “The principle of integrity imposes an obligation on all professional accountants to be straightforward and honest in professional and business relationships. Integrity also implies fair dealing and truthfulness.” "1102. Professional accountants should not be associated with reports, returns, communication or other information where they believe that the data; a) consist of a materially false or misleading statement. b) involves statements or information furnished recklessly. c) omits or obscures information required to be included where such omission or obscurity would be misleading. “
Objectivity	A continuing duty to maintain professional and skill at the level required to ensure that a client or employer not to compromise their professional or business judgement because of bias, conflict of interest or the undue influence of others.”
Professional competence and due care	"To keep professional knowledge and skill at the level required to ensure that clients or employers receive competent professional service and to act diligently by applicable technical and professional standards when providing professional services."
Confidentiality	“This requires disclosing information needed as a result of professional and business relationship outside of appropriate and definite authority or unless there is a legal or professional right to reveal it."

Source: (International Federation of Accountants, 2005)

From the above table the four main professional, general application of accounting code of ethics is listed and explained. A professional accountant is obligated to abide by the fundamental principles. Within the integrity principle, a professional accountant should be honest and truthful in all competent and business affairs. The objectivity principle stipulates that a professional accountant should not allow favouritism or preferences, incompatible concerns or aims of two different parties to supersede professional or business decisions. Professional competence and due care, it is the responsibility of an accountant to keep expert knowledge and skill controlled the level obligatory to guarantee all parties involved receives adequate service based on current development in the standards. Under the confidentiality principle, the privacy of information gained should be respected and should not reveal any information to third parties without permission unless legal or professional right or duty to divulge any information. (International Federation of Accountants, 2005)

1.2 Concept of Creative Accounting

The terminology of creative accounting (CA) can be interpreted in many ways; it is based on the angle and context in which it is taken. Creative accounting is using the flexibility within accounting to govern the evaluation and the appearance of the accounts so that it will best represent the welfare of the management and their corporations (Jones M. , Creative Accounting, Fraud and International Accounting Scandals, 2011). Creative accounting is also known as a system of accounting which, although abides by the rules and regulations, it stills presents a partial image of excellent performance by a company. (Jones M. , Creative Accounting, Fraud and International Accounting Scandals, 2011). "In summary, it is a mechanism through which accountants use their knowledge of accounting rules to exploit the figures in the account of a business" (Amat, Blake , & Dowds, 1999).

“The 25th chairman of Securities and Exchange Commission brought light to the topic of creative accounting habit and declared an all-out war on them. He acclaimed that accounting principles were not meant to be a restriction and some degree of flexibility was fundamental to allow financial reporting to maintain unity with business continuing success. As reported by him, the issue emerges when companies are adopting that flexibility to establish a false image of their financial reports, false images that are not true reporting.” (Demirhan & Susmus, 2013)

Even though creative accounting is a popularly used term, it is explicit definition is not agreed upon by many. The truth is the phrase can be broadly defined. In the United States creative accounting is seen as including fraud whereas the United Kingdom sees CA as using the flexibility within the governing system, however, does not cover fraud. It can be characterised as applying the flexibility in accounting inside the governing framework to control the evaluation and appearance of the accounts to ensure they bestow the utmost importance to the interest of the preparers, not the users' (Jones & Jones, 2011).

Based on the knowledge of the author, the creative accounting practice which is used not necessarily bad intentions but to protect the integrity of a company or management. However, one has to wonder, with so many cases of related incidents becoming more aware to the public, why does the practice of creative accounting continue to be practiced? Are managers and accountants not thinking of the long-term consequences or are they confident that the loophole being used will not bring about any adverse effects, or merely that they have the perception that the parties involved are not educated enough to understand the manipulation methods that are being used. If professional accountants are supposed to follow the accounting rules of ethics how then is creative accounting is such a standard issue, one would have to wonder if the ethics of the practice is just a perception based on individuals and not actually in accordance to the accounting ethical standards.

1.3 Main Functions and Methods of Creative Accounting

“Creative accounting may be practiced through the selection of accounting policies a firm implements in the preparation of its financial statements or the way in which those accounting policies are applied. An availability of flexibility in accounting policies allows this practice to be done. The selection and application of the accounting standards, GAAP or IFRS is flexible, opening the opportunity for judgement in some special cases.” (Mulford & Comiskey, 2002). According to some, there are two main types of manipulations; these are based on the users of the financial report. To manipulate against the firm and to shape for the firm. Manipulating for the firm is done on behalf of the firm, to give investors or other external the false image of their actual numbers. (Mulford & Comiskey, 2002) Then there is manipulation against the firm is to target the internal users such as shareholders, this may be done to attain some greater compensation or earnings. This relation is reflected in the figure below.

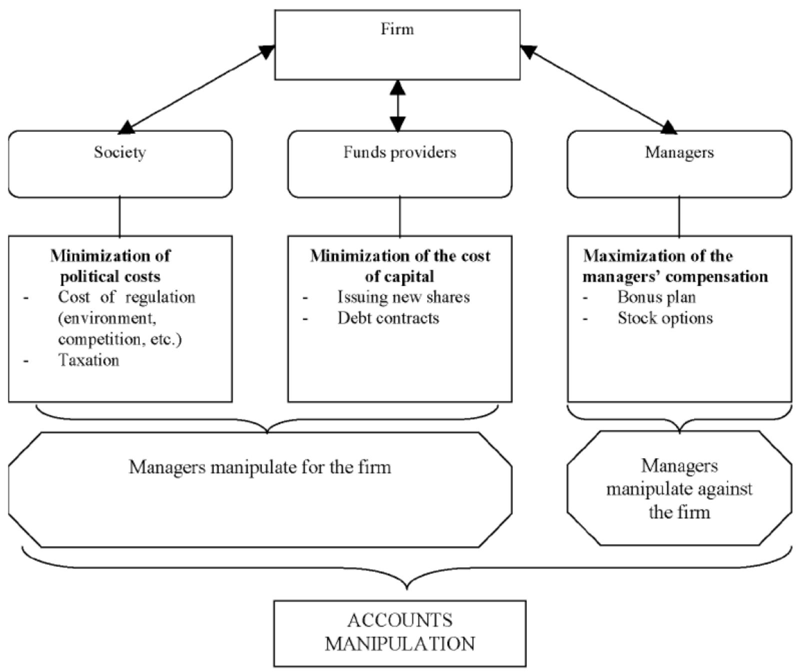


Figure 1: Principles of Account Manipulation
Source: (Sakkal & Nadim, s.a)

The IASC's framework for the arrangement and production of the financial statement, pictured by the IASC is presented in the following group of users; employees, suppliers, creditors, clients, the general public, governments and also current and potential investors. Following the position of the user's relationship to the frim, they may be divided into two groups, internal and external. Internal users are those who are in the management position of the frim; these are the one who manipulates against the frim because they have a responsibility for information release system and thus have access to additional data about the firm. While external users are those, who can dictate the nature of the of the data which they only have access to, examples of these are banks and governments, the external investor's limitations are based on authority. (Balaciu & Vladu, s.a)

There are various methods to the process of creative accounting which are expressed in four groups.

1. The rules of accounting give way for firms to select a variety of methods. They are allowed to choose the method which presents a preferred result or outcome.
2. Within the line of work for accountants a significant level of forecasting, perception and evaluation is present. For instance, when calculating depreciation of an asset, firms usually choose the method which is of more significant advantage to them.
3. Employing the use of fake transactions can change the amounts reported in the balance sheet and may also move profits between accounting periods. This method may be attained by including more than one deals and with a third party being involved.
4. Business negotiations can be timed base on the corporation decision, this way an image is formulated to express it favours the accounts. (Sakkal & Nadim, s.a)

With the various methods to the process of creative accounting, it is a risky practice and also a costly one and those involved usually try their best to be careful as possible. With the first method it is widespread for loopholes in all aspects of life, as humans, we like to bend the rules and search for ways to get around them to limit the restrictions these rules impose on us, we like the feeling of beating the system and finding a way to benefit still. From the second group of the method through a significant level of forecasting and estimation is needed, it brings about the issue that accountants who manipulate on behalf of management may use this reasoning as an excuse for the numbers presented in the financial statement.

Methods

- Increase Income (incomplete sales recognition)
- Decrease Expenses (provisions accounting, capitalisation of interest)
- Increase Assets (increase goodwill, revalue fixed assets)

- Decrease Liabilities (off-balance sheet financing, reclassifying debt as equity) (Jones M. J., 2015)

In the next section below, I will expound on each of the above methods, giving examples of explaining more about how they are achieved.

1.3.1 Increase Income

The IFRS 15 formulates the standards that a body implements when reporting information on the recognition of revenue. With the IFRS to recognize revenue under the IFRS 15, five steps need to be administered before revenue can be recognized, first a contact must be identified with the party involved, then the promises or agreement of the contract must be acknowledged, the next step is determining a transaction price of the service or product render followed by a distribution of price to each obligation made in the contract and the final step in the process is to recognize revenue when an obligation or promise is completed, and the client is satisfied with the contract obligations being met (IFRS Foundation, s.a). Under the GAAP, revenues can be recognised from the sale of goods if you are capable of ensuring that the agreement made in the contract based on a fixed fee that you are sure to collect. With the GAAP, if the service includes a contract that has more than one component, the recognition of revenue must wait if there that a refund may occur, because all components of the contract were not able to be delivered or met. However, the IFRS it is possible for revenue to be recognised in advance when some of the obligations have been completed. (Bank, s.a)

Increasing income is one of the most common methods used by the public firms who are seeking to improve their income is to recognise their revenue before actual work is completed, or plainly to formulate sales. The problem is when exactly is revenue to be identified changes vastly, but at the end of the day, the main criteria are where the payment and the delivery of goods are guaranteed. (Kuepper, Creative Accounting: When It's Too Good to Be True, 2018). The overvaluing of the closing stock by decreasing COGS will result in an increase in profits and also total assets on the balance sheet. Using Microsoft Corporation as an example of recording revenues at any moment from the time of sale contract has been made to the time the service or product was delivered to the customers. The U.S Securities and Exchange Commission found that Microsoft had only recognised 20-30% as revenue at the time of sale and the remaining amount was kept as provisions for the future after sales services. (Zulfiqar, Shah, Butt, & Tariq, 2011). Looking at Xerox Corporation, within three-year time span they were fined for the reason that they inflated revenue by $2billion. Xerox had set up reserves for items such as vacation pay, growing the balance sheet within bad years, then releasing the reserves in the better years. This strategy aided in improving the earning during the years when business was bad, according to the securities and exchange commission." (Pulliam & buckman, 2002).

Other ways include companies changing the estimated sales. This method will result in higher sales and earnings being reported as higher than they are. The reporting of revenues can be challenging, as not all auditors argue alike when an item should be recorded as revenue. Hence manipulating the sales estimate to be reflected in a positive appearance tend to deceive investors. (Sakkal & Nadim, s.a)

1.3.2 Decrease Expenses

According to the business dictionary, expenses are "monies spent, or cost that arises in an organisation's attempt to achieve revenue, characterised by the cost of doing business. Expenses are presented in the income statement as a reduction from the income before the evaluation of income tax. (Business Dictionary, n.d.)

There are various approaches which are used to keep expenses under control. However, they are a few basics which can help limit the costs that are reported. Expenditures can be capitalised and moved straight to the balance sheet as part of the associated asset. They can be allocated, which is a difference on the capitalisation line and usually involves cost being handled directly through reserves which the firms do not under-provide for (Griffiths, 1995). Through decreasing expenses, profits are generally increased. More ways in which this is done is by capitalising expenses as interest payable for them to be recorded as assets and not liabilities. Moreover, it is possible to extend the lives of assets as a means of decreasing depreciation. According to an excerpt from Accounting and Companies Performance Management (Bohuslava, 2002), the method of depreciation effects the cost of the firm and fascial outcome of the firm, management also controls which methods should be used, a systematic or consistent approach, or a faster or slower method of depreciation. Expanding inventory, decreasing taxes and using the prominent bath methods are also ways of reducing expenses too. The important bath charges method is a way of showing all loses in one year by charging all expenses in that year due to deficient probability in the same year, which will ultimately result in better profits to present in the following years. (Zulfiqar, Shah, Butt, & Tariq, 2011)

1.3.3 Increase Assets

It has already been stated that decreasing expenses will increase assets. Other ways included the way of increasing the value of intangible assets and adding them to the accounts, and also the revaluation of tangible fixed assets accounts. (Jones & Jones, 2011) “Companies report current asset-period expenses and or losses as assets. As a result, expense recognition is postponed, boosting current-period earnings. (Mulford & Comiskey, 2002)

An additional way of reporting greater earnings is, by over evaluation of an asset is another way of increasing assets. Inventories are used in creative accounting to provide a more attractive result. The selection and application of a peculiar depreciation method in a methodical way of an asset during its useful life affects the profit and loss. In this manner, various methods of depreciation have different effects on the outcome. (Moeller & Landry, 2009) Contingent upon the depreciation method chosen the time allocation of payment can be changed. The alternative of utilising different useful life results to different payments. A revision of useful life usually results in cost adjustments with the present and future depreciation period. Reducing the residual value has the impact of lowering depreciation and thus increases the outcome, resulting in increased assets value.

1.3.4 Decrease Liabilities

An additional approach to improving the final assets is through decreasing liabilities. The couple generally known approaches are by off-balance sheet financing and reclassifying debt as equity.

Off-balance sheet financing seeks to isolate debt in additional companies of the parent company, which are not then consolidated or combined.

The manner in which companies report bad debt, may also be an example of how debt may be decreased. The earnings will be higher, the lower the estimated bad debt is. Hence companies result in reporting the least possible amounts of such debts. Bad debts may be estimated by an allowance method ant the ageing method. The allowance method is calculated as a percentage of the account receivable balance. Moreover, the ageing method which is based on the presumption that the more time an account balance is tardy or outstanding, the least likely is the probability that the debt will be paid, so companies resort to having an account receivable ageing schedule. Companies also used the percentage of credit sales method which estimated bad debt as a percentage of credit sales. This percentage method disregards any leaving balance in the allowance for bad debt accounts. (Sakkal & Nadim, s.a)

Some companies also fail to make a record of contingent liability. “Contingent liability are responsibilities that are reliant on future events to affirm the existence of an obligation, how much is owed, the date payable or payee. The failure of a company to record such a liability that is expected to be earned and subject to reasonable estimation is understanding their liabilities and overstating their net income or shareholders' equity. Entities can creatively give a reason for these liabilities by understanding their materiality." (Kuepper, Spotting Creative Accounting On The Balance Sheet, 2010)

1.4 Reasons for Creative Accounting

They are many motives for managers to practice creative accounting within their firms. Many times, the main reason for the improve the firm's share price. For others, the motivation may be an appetite to enhance debt ratings and reduce interest cost on amounts previously borrowed or to create an image so to better reduce the restriction from debt agreements. The idea of improving a profit-based bonus may be an incentive to some. "Internally CA practice is done to meet internal targets; the managers want to prepare the books to meet internal targets set by higher management concerning sales, profitability and share price. Externally a firm has to face many expectations from its stakeholders. The employees and customers want a long-term survival of the company for their interest. Suppliers want assurance about the payment and long-term relationship with the company. Companies also want to meet analyst's forecasts and dividends payout pattern. Firms may also want to show a stable income flow to impress the investors and to keep the share prices steady. About creditors and IPO window dressing is done. The creative accounting practice may also be a result of a desire for some tax benefits especially when taxable income is measured through accounting numbers." (Syed & Butt, 2011)

Creative accounting is usually practiced bringing together the interest between various groups. Various groups in society attempt to enlarge their own utility. One of a manager's internal goal is to pay or avoid as little taxes as possible while reporting increased profits so that they may receive a more significant bonus from the firm's bonus scheme plan. Another motivation for creative accounting is because shareholders expect high dividends and internally employees receive an improved income and larger profit share. Moreover, concerning government, they will receive higher taxes on collections.

Within IPO firms they are stimulus which prompts them to increase earnings in the period right after the IPO. It is usually the likelihood of a high after-market price increase that the possibility exists that the offering will be fully subscribed, which enhances the possibility that the underwriter will be willing to accept the offer price. The underwriter pledges the issue proceeds in a firm commitment offering, and risks to lose if the issue is undersubscribed because of the offer price is set too high. Firms may also be under pressure from investment bankers to support the stock price after the IPO because the investment banker buys the stock of the firm to improve the offer price in the aftermarket. (Teoh, Wong, & Rao, 1998)

Before continuing to the next section of this paper, a visual representation of some of the world's biggest creating accounting scandals is displayed in the table below. The table aims to give an illustration of how each company went about with their creative practices and the outcome of each scenario, with the intention of linking the idea to the theoretical information mentioned in the above chapter.

Table 2: Companies that implemented creative practices and how they did it.

Company	Location /When	What happened	How they did it
Enron	USA/ 2001	Shareholders lost $74 billion, thousands of employees and investors lost their retirement accounts, and many employees lost their jobs	They kept large amounts of debts off of the balance sheets
WorldCom	USA /2002	Inflated assets by as much as $11 billion, leading to 30,000 lost jobs and $180 billion in losses for investors	WorldCom underreported line costs by capitalising rather than expensing and increased revenues with fake accounting entries.
Royal Ahold	Europe/2002	Profits were overstated by more than €463m, in two years. It is market value plunged by 63% on February 24th, 2002, IN late 2001 it exceeded €30 billion.	"During the bubble, Ahold started claiming profits of acquired firms as organic growth, booking capital gains from sales and leaseback deals as profits and keeping billions in debt off its balance sheet" (The Economist, 2003)
Tesco	United Kingdom/2014	£263m profit overstatement	Executives were pulling forward payments to paint a more flattering picture of the supermarket's finances

Sources: (Butler, 2014) (Farrell, 2015)

The table 2 above shows real-life examples of some companies around the world and how they applied creative accounting practices and the outcome of the practice. Off-balance sheet debt seems to be a conventional method. With off-balance sheet usually, assets or liabilities items are left off the balance sheet; these may be anything that a company does not claim to be legal owners of or no responsibility for such as operating lease, they are also difficult to identify in a company's financial statements. These, however, must be repaid sometime in the future. (Business Dictionary , n.d.)

The credibility of accountants and financial analysis are bound to be destroyed after scenarios like those in the above table. Due to the immensely advertised financial frauds and lack of success, irresistible questions have been brought up about the duty of public accountants. Due to these cases, the practice is being looked into, and the ethical aspect is being researched upon (Jooste, 2009).

1.5 Accounting Ethics

Learning accounting ethics at higher education and the involvement of accounting concerns within business ethics development precede the current phenomenon of international business scandals and accounting failures. In the 1980s, an academic article, begun calling for changes to be made to ethics in the profession and encouraging ethics teaching in accounting education. The study concluded that the teaching strategies need to be addressed and who is responsible for teaching accounting ethics courses, the question also arises on whether adequately ethics can be adequately taught to university student (Stuart, Stuart, & Pedersen, 2014).

“Elias (2002) assessed students, faculty, accountants in the industry and certified public accountants (CFAs) and noted that accountants in practice were more tolerant or allowing than accounting students and faculty were.” (Stuart, Stuart, & Pedersen, 2014)

From the author's point of view on the subject of accounting ethics manipulation, maybe the accounting codes of ethics or accounting standards are not rigid enough, hence why loopholes are continually being found and applied, another side of the spectrum is what if these standards are also too strict hence resulting in the creativity of the practice.

2. RESEARCH DESIGN AND METHODOLOGY

In this chapter, the author explains the preparation and description of the survey and compiled results from questionnaires. Sample designs are presented, and the reason for choosing the method and questions is explained. These surveys were structured in a way to understand the perspective of the target audience on the subject and the driving force behind their reasonings. The questions present in the survey part of this paper was formulated based on questions from a previous survey on a similar topic. The author finds the questions best suited for this research as they set out to explore the opinions of current students who may become potential managers, accountants or investors.

2.1 Survey method and data collection

For this study, the target audience included accounting professionals, students and scholars in the accounting and finance field of research and also other professionals within the business environment who are directly related to the subject of creative accounting and even those who are potential future professional in the field. Exploring the accounting ethical perspective of creative accounting would be best expressed by this group. A Google form questionnaire was designed and sent out electronically by email to ten current accounting professionals, where then the author asked those individuals to share the survey among their collogues, the form was also posted on various social media platforms, making it difficult to pinpoint the exact number of individuals the questionnaire reached. The author though this means of distribution was most suitable as the aim was to get as many diverse responses from different cultures around the world.

2.1.1 Questionnaire Design

Some of the questions were adopted from a previous research paper titled; “survey of creative accounting practices: an empirical study.” (Bhasin, 2016) The author felt that the questions adopted were well suited to carry out research on how current and potential users of financial statements view the ethical satiation of creative accounting. The author also formulated his own questions based on the nature of the paper to gather diverse opinions of the different respondents. The literature review was also a platform for developing the questionnaire questions.

Unfortunately, the author was only able to receive feedback from 50 individuals, making it difficult for the author to present a response rate percentage. Due to the limited response to the questionnaire, the author must point out that the respondents who participated do not represent the opinion of all accountants, accounting and business scholars, students and managers. Majority of the respondents were hesitant on giving their full opinion, resulting in a few unanswered sections of the questionnaires. As stated in Business Research Methods, "response rates differ extensively based on some things, the connection between the interviewer and the target audience, survey length, understanding, reasons for responding and of the topic. (Cooper & Schindler, 2013).

A total of 17 research questions were proposed to the participants, the questions aimed to explore the opinions and viewpoint on the ethical behaviour of the creative accounting practice. The survey was done anonymously, and the identity of all responses expressed was confidential. The results are presented in table form below.

The questions were strategically formulated and orderly placed to ensure the perspective of the respondents were suitable for the study and also to provide the respondents were comfortable and open in giving their feedback. The primary focus of the questions was to get background structuring of the participants, knowledge of the topic on creative accounting, opinion on the topic and their attitude towards the ethics of practice by incorporating a short situation case on how they would behave within a given situation.

2.1.2 Demographics analysis

Table 2: Demonstrates the background of the respondents

Respondents	Demographic data of the respondents (%)	
Gender	Female	52.4%
	Male.	42.9%
	Prefer not to say	4.8%
Geographical location	North America.	28.8%
	Latin America	17.4%
	Asia	9.5%
	Europe.	31.3%
	Other	13.2%
Profession / Specialty	Accountant	31.7%
	Manager.	17.5%
	Audit	4.8%
	Students (Financial / Accounting)	46%

Source: Prepared by the author

The author chooses to include location as a question due to the reason that in the U.S creative accounting may be seen different from Europe and other parts of the world. "According to a UK based dictionary, Black's Law Dictionary, 7th edition, 1999 it classifies creative accounting as using accounting flexibility, which excludes fraud to present and measure the financial statements while the American definition of the term incorporated fraud as part of the meaning. Which makes it more illegal in the eyes of the American law." (Popescu & Nisulescu, 2014)

As it is seen from the table majority of the respondents are currently located in Europe with a 31.35, followed by the North America with 28.8%, Latin America with 14.4%, the survey also received a 9.5% response from Asia and 13.2% from the other category, unfortunately the author was unable to identify the location of this group, which surprisingly had more respondents than Asia. Nevertheless, a broad scope of individuals was reached which will give more diverse responses to the questionnaire.

About the profession and speciality of the individuals who responded, the most significant amount of responses was seen coming from scholars who have studied or is studying in accounting and or finance related field with 46%, while there were a reasonable number of respondents currently working as accountants which totaled to 31.7%. Managers amounted to 17.5% and auditors at 4.8%.

3. Results and Findings

Table 3 Awareness of the term creative accounting.

Answer	Percentage (%)
Yes	38.1%
No	28.6%
Maybe	33.3%

Source: Prepared by the author

This question was proposed first as to check the awareness of the term without having to explain it, later in the questionnaire the term was defined.

The results show that more than average was aware of the term. Using this information, the author implies that the following research questions should receive more expert knowledge on the topic. The author also makes notice to the fact that out if the 49% of scholars only a possible 9% were unaware of the term creative accounting or maybe they have heard of it but did not know what it is about. Hence, thee maybe option in the question.

Participants were then given the definition, "the term creative accounting is using the flexibility within accounting to govern the evaluation, and the appearance of the accounts for it to best represent the welfare of the management and their corporations" (Jones & Jones, 2011). The participants were then asked to give their feedback on how they viewed the practice, based on the definition given and three options of either it is good, bad, or they cannot say.

Table 4: Perception of CA definition

Answer	Frequency (%)
Good	38.1%
Bad	23.8%
Cannot Say	38.1%

Source: Prepared by the author

Based on the results almost more than average said they thought the practice was good. A shocking 38.1% indicated that they could not decide on whether the practice was good or bad, thus the author suspects the results are based on the accounting ethical background of those who could not decide.

When participants were asked, "from your perspective, how would you classify the practice of creative accounting?" A significantly large amount of 42.9% insisted that they did not know how to classify the practice, 38.1% considered the method of creative accounting to be legal and totally legal, 19.1% had a perspective of CA being just illegal and totally illegal. From the data, we see that majority of the respondents did not know how to classify the practice, which may suggest that they are not as familiar with the accounting ethics guidelines or based on their perspective they may see CA as a valuable tool, but still battle with the ethical factor of using the practice. There was also a considerable amount who viewed the method as legal. The author uses this information to assume that this makes it easier for managers to ask or have accountants assist them in the CA practice.
The data is presented in the table below.

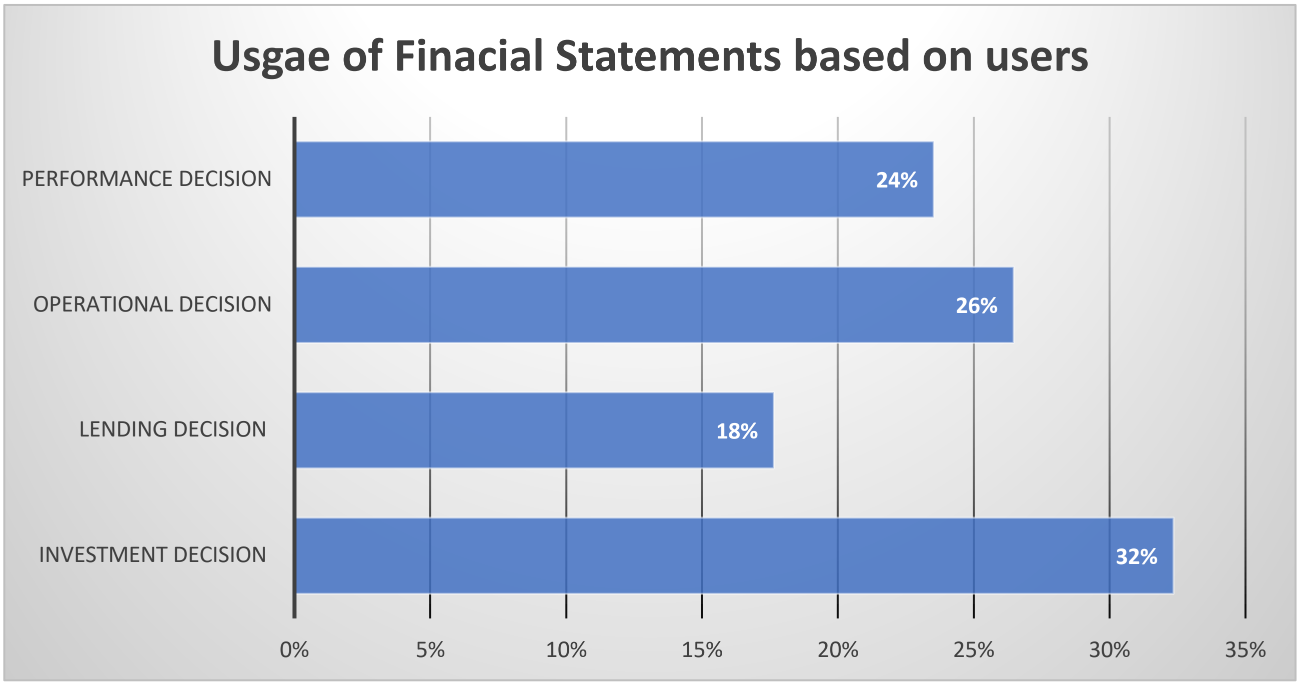
Table 5: The Legal position of CA practices based on the perceptions of financial statement users.

Questions	Frequency (%)
Totally Legal	4.8%
Legal	33.3%
Totally illegal	4.8%
Illegal	14.3%
Do not know (cannot decide)	42.9%

Source: Prepared by the author

The next statement presented to the respondents is concerning finding out what information the users are seeking mostly from financial statements. The question proposed was "If you do, for what reason do you use financial statements?" Four main options were given, which are; for investment decisions, lending decisions, operational decisions or performance-based decisions. Respondents had the option to select multiple options as they see fit. Based on the respondents more than half of the responses, investment decision was the leading reason for using the information presented in financial statements with a frequency of 32%. One would argue that this would have been the number one reason and it is also seen as prevalent in comparison to the respondents. Trailing behind with the second largest was the option to make an operational decision with a 26%. With a considerable amount of 24% indicated that they mostly used the information from financial statements to make performance-based decisions, which means that they wanted to see how the company is doing performance wise. So lastly with a frequency of 18% usage of the FS was to determine lending decisions. See diagram below for visual reflection.

Figure 2: Usage of financial statements based on its users.

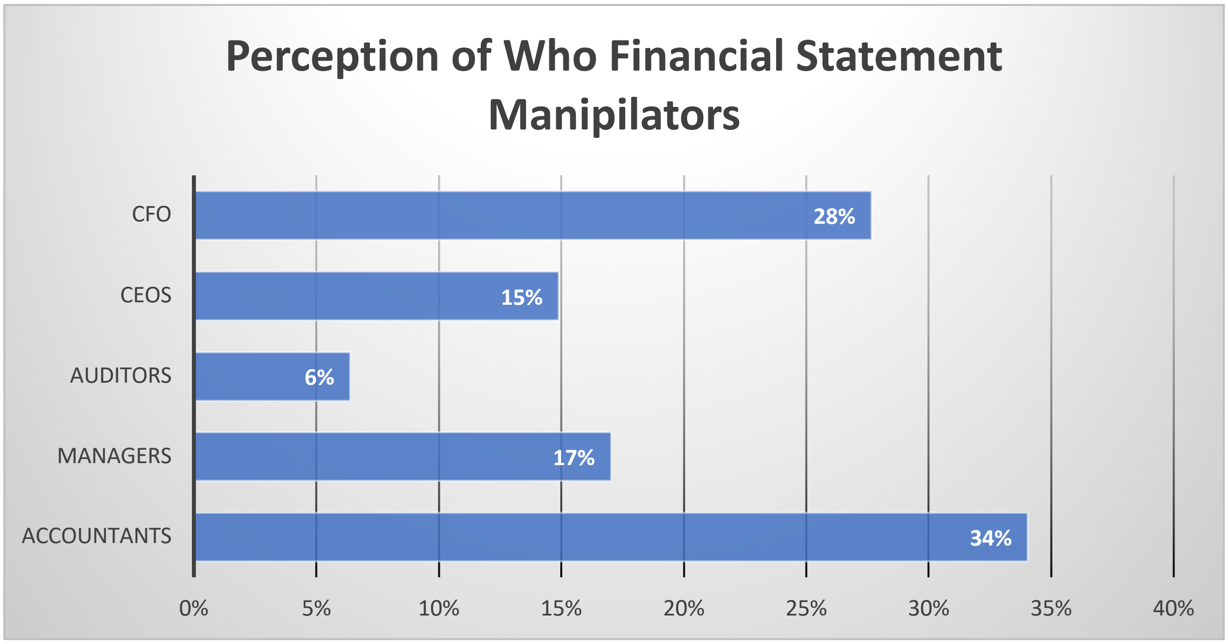


Source: Prepared by the author

Here the author makes a correlation to the theoretical part of this paper and makes the assumption that if information on investment decision is what is most sought after from financial statements then again investors are mostly affected when creative accounting is used. We have also seen cases in where the practice has been used to present a false image of the performance of a company. Hence those who are seeking performance-based and operational decision will inevitably receive false information.

In the next question, the author sets to determine whom the accounting and related professionals perceived to be the primary critical manipulators of financial statements. Based on theoretical data, often the manipulation of financial statements are done on the request of managers. Thus, resulting in creative accounting practices being implemented. The next questions proposed asked participants, whom do they believe manipulates financial statements. Responses are displayed in the following chart.

Figure 3: Perception of Who are the financial statement manipulators.

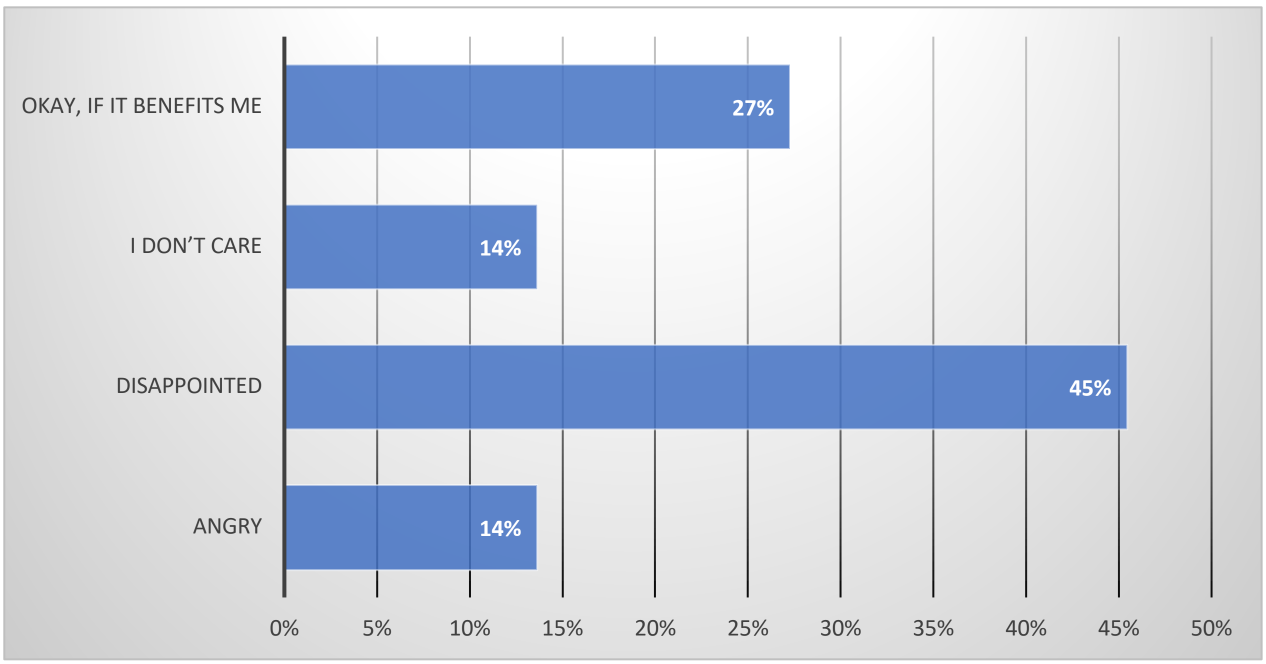


Source: Prepared by the author

From the information, we see that the most perceived chief manipulator is the accountants with a frequency of 34%, while CFO ranked second with 28%. Respondents said they believe 17% of managers manipulated financial statements, whereas 15% selected CEOs and lastly auditors received only 6%. Although the perception shows accountants as the main culprits of financial statement manipulation, the author uses his knowledge to question the results as top managers and CFOs stand to benefit the most from the manipulation both from the internal aspect and external. These top managers than in turn request from their in-house accountants to manipulate numbers. So ultimately managers are the driving force behind the accountants to perform creative practices.

To gather the opinion of how the respondents in the related field and those directly affected, a question was proposed to get the feedback on how they would feel or react if creative accounting practices were used and it affected them as investors. The question asked, “If you were a stakeholder or investor in a particular company and you found out the financial statements were manipulated through creative accounting practices. How would you feel?” Four options were given, from being angry, disappointed, not caring and to the option if it being okay if it benefitted them. Based on the responses the question received 45% indicated that they would feel somewhat disappointed. Ultimately, they would because they may be investing their money and time into a particular business for positive returns only to find out later that the business is going bankrupt or other effects of using the practice. 27% said they would have been okay with the practice if it benefitted them. This high response gives the author the impression that some of the respondents are unaware of the effects of CA practices. Also, 14% indicated they did not care and that they would be angry. Data is presented in the chart below.

Figure 4: Ethical perception of creative accounting practice.



Source: Prepared by the author

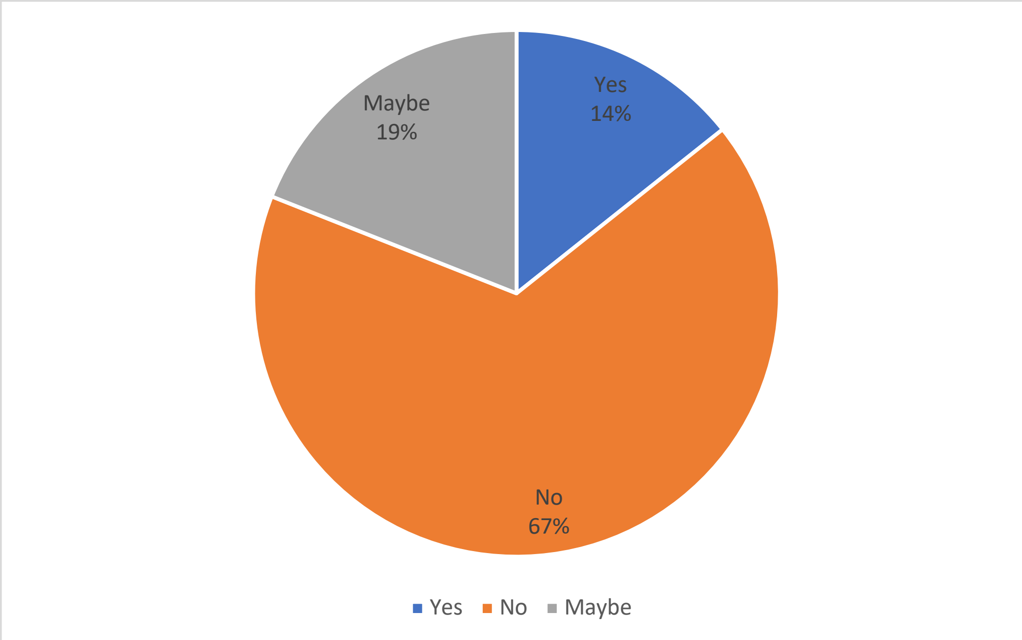
The following question is related to the previous question. The respondents are asked to explain their reasoning for their choice of answers above. Here the author summaries the response received. For most of the disappointed and angry responses, their main reasoning was that they believe a company should display their accurate financial at all times to prevent misrepresentation to their investors and shareholders, some argued that the practice is just plainly not honest, and ethics is fundamental in any work-line, especially accounting. One respondent indicated that they would be angry because it is "likely that if a person is to benefit from creative accounting, they may not have a problem with it, but on a moral level if others are being taken advantage of because of these

practices, it may cause me to feel guilty and dishonest." Another main reasoning was because respondents felt that manipulation of financial statements means that there will be overstated or understated amounts, which doesn't give an accurate reflection of the company, thus enabling misrepresentation of decision making. Moreover, they would not like to be losing out on money nor the value of their investment. Some aired that the practice seemed unethical.
Others who did not care much or indicated that it was okay if it bothered them, reasoned that it might be necessary for the survival of a business and they understand the rationale behind the practice. Some also argued that once the method being used is considered legal or ethical, they are okay with it. Some plain out said, "if it works, it works" indicating their approval and saw nothing wrong with it.

As stated in the theoretical chapter of this paper on accounting ethics, the author makes a correlation to the issue that accountants are more open and allowing to creativity in the numbers than students and scholars, who were stricter on the issue, students and scholars favour to judging the practice more ethically, this may be due to the fact that they are using their personal ethical feeling because they were never thought on the topic of accounting ethics.

The next proposed question was "if you were a manager, accountant, of a particular company, would you manipulate financial statement through creative accounting practices?" A considerable large amount of 66.7% said no they would not, while only 14% indicated that they would, and 19% was undecided with maybe. A representation of this data is presented in the next chart.

Figure 5: Displays whether or not respondents would manipulate financial statements.



Source: Prepared by the author

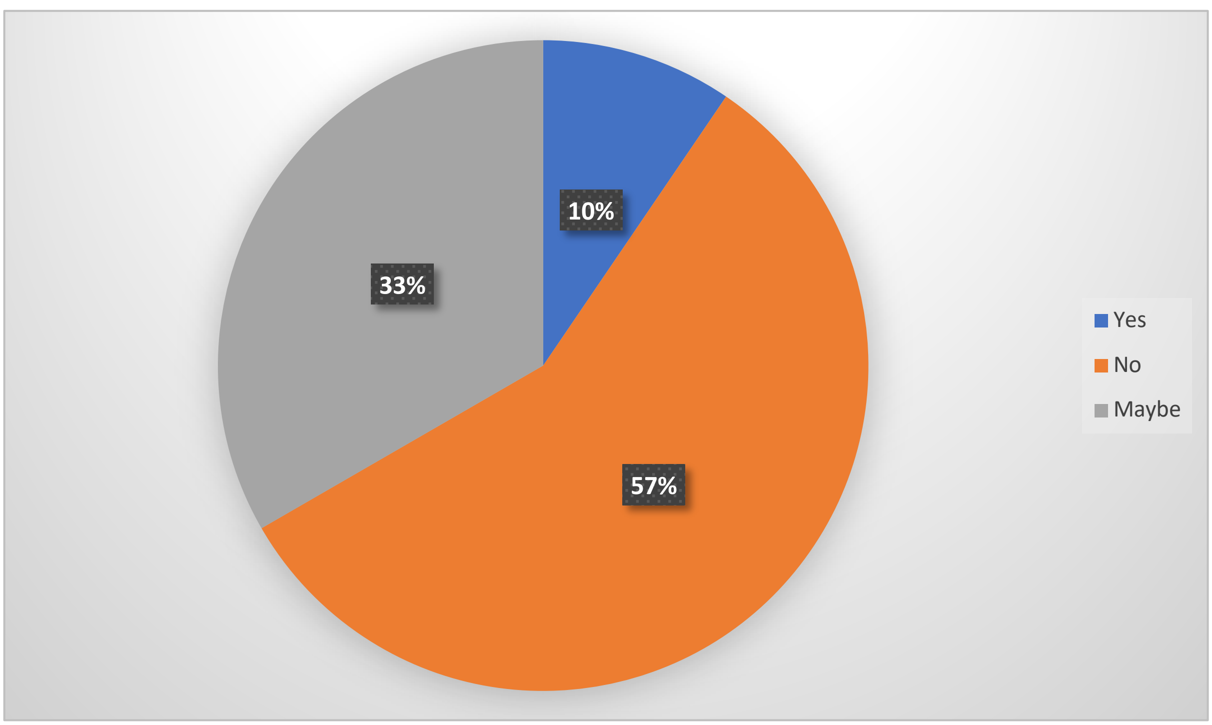
The following is a summary of the reasoning of the decision of the respondent's decision to the above question. For the most extensive response of no, the main factors were that most of the reactions what that the respondents did not believe it was right, some said it was against the law and may be illegal, other indicated that they think the practice is unethical and they would not lie. Some of the reason also mentioned were that some see it as being deceitful and wrong. Moreover, lastly, some wanted the company to reflect its actual position and wanted all personnel related or affected by the accounting practices and decision to feel like it was fair to all parties involved.

Those who agreed that, yes that would manipulate financial statements said that their reasons are because if their superior, boss or CEO asked them to do it, they would do it. Others said if it was within the confines of the law, then, by all means, it should be done to maximise business performance, another central point expressed what that if the practice was not illegal and management required that they manipulate something then they might do it. One individual indicated that if they needed to attract investors, then they would have no problem practising such practices. Lastly, others who said maybe choose to leave no comment on their reasoning.

Again, here we see can conclude that majority of the no response came from the largest group within the survey, the scholars and students. This response may also be influenced by general the fact that this group of individuals depend on their feelings of what they perceive to be wrong or right since they are not as experienced on the accounting ethics principles and standards. The option of maybe and yes, amounted to a total of 33% together, the author is assuming here that given the definition this group though perhaps it is worth the practice if it benefited them and also the reasoning for their decision could be depending on where they are from and how in their minds the definition is perceived, whether is more on the fraud side or the just the flexibility side of things.

For the next question, a scenario was proposed, "If a business failure was on the brink, meaning employees will be unemployed and the company faces bankruptcy will I then be okay to use creative practices?" 57.1% insisted that it was still not okay, while 33.3% said they maybe consider it and 9.5% expressed that they will implement the creative practices. The chart below displays the responses.

Figure 6: Scenario response on whether or not a specific situation may motivate the need for manipulation.



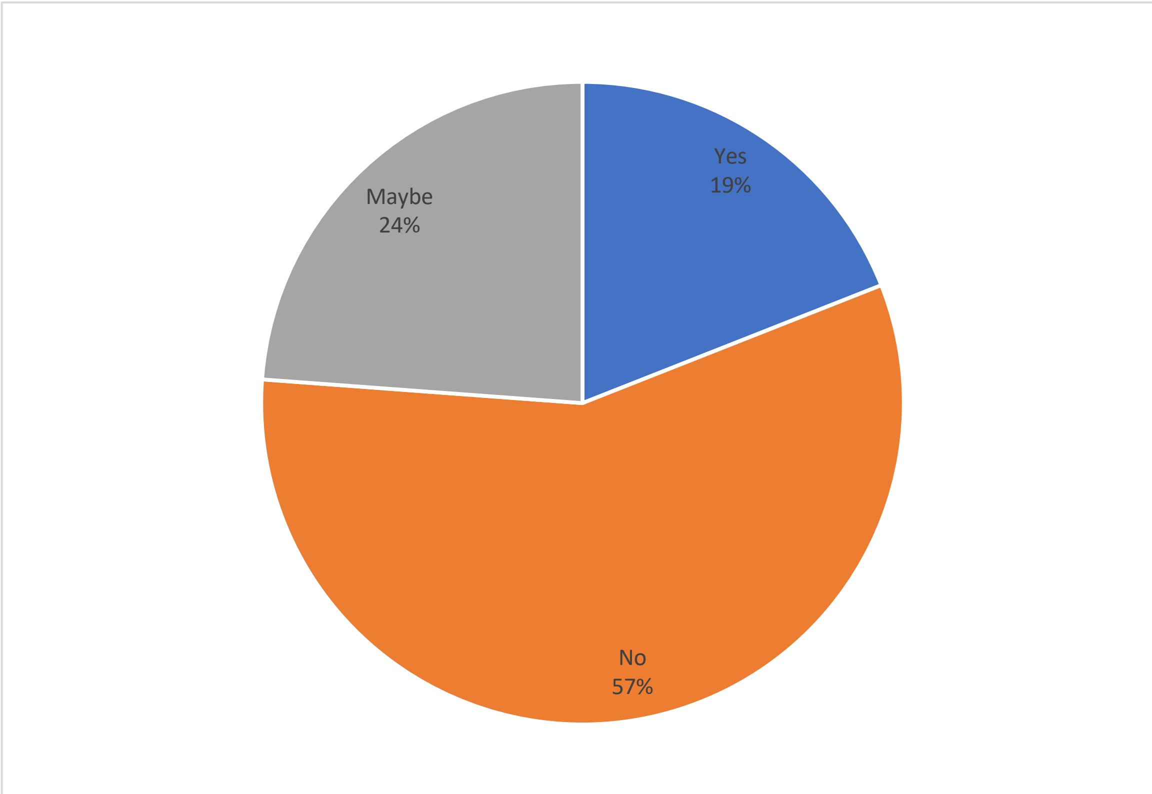
Source: Prepared by the author

From the previous chart a significant amount of respondents are still undecided as to if they would actually implement a creative accounting practice, the reasoning for this may be due to the reason that some accountants actually and managers are actually following the rules of ethics, also since majority of the respondents were scholars, they have no idea of the pressure of such responsibilities and they find it easy to say no, or maybe at the moment because they are inexperienced and not in that position to make the decision. It is always easy to same one thing when you are not directly facing the situation, but when one is faced with the situation, their thoughts change.

In the next question, the author asked an open-ended question; the question was "do you believe any situations may justify using creative accounting. The responses received for this question were not well received as most of the respondents choose to reply with either yes or no. However, a summary from the usable reactions, some indicated that in cases for tax evasion they believed the practice was justified using, some said if it was in the interest of the managers, others expressed that once it was kept within legal terms, then it was justifiable. A few individuals also indicated that they do not think creative accounting is essential, and individuals who practice should adhere to the international standards of accounting rules.

The author now wishes to indicate here that based on the theoretical part of this paper, it was already shown that they are many reasons why managers may implement the use of creative accounting. Ideas such as for the need to keep their position within a company, also to attract potential investors and to for their benefit towards creditors, but due to the nature of the group of respondents the reason for such a significant response of no, may be due to majority of the respondents are not currently looking at or dealing with financial statements or in the position to implement the practice of creative accounting.

Figure 7: the expression on whether or not the respondents believed that accounting standards are too rigid and force creative accounting due to their view of conservatism.



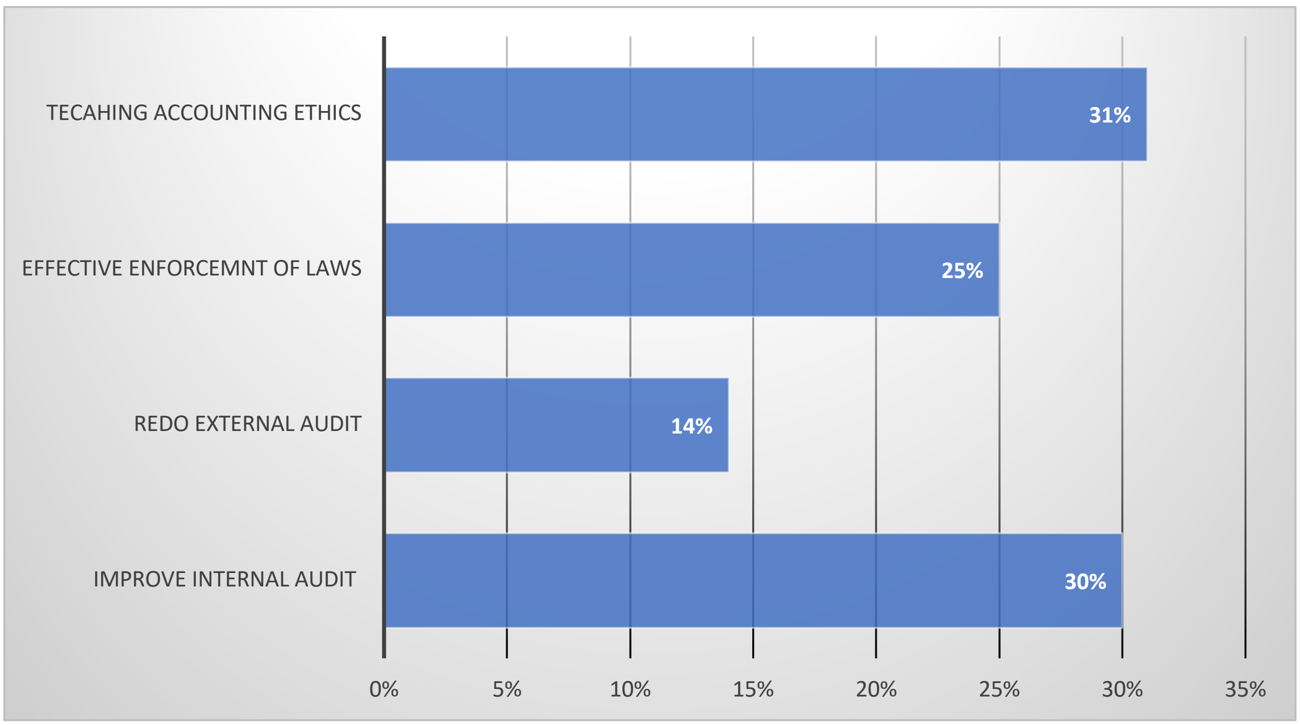
Source: Prepared by the author

From the chart we see that a considerable amount of 57.1% indicated that they do not believe the accounting standards are too rigid and do not force creative accounting, 23.8% said maybe it is while 19% agreed that it is too rigid and may be the reason.

In the final analysis question, the author tried to see which general ways or practices may best prevent or limit the exercise of creative accounting. The question proposed was, "which you believe would be the best way to reduce creative accounting, in your opinion. Select as many." The options provided were as followed, improving internal audits, redoing external audits, effective enforcement of laws (accounting rules and regulations), and lastly by teaching accounting ethics to students and accountants. The responses are shown below in the chart.

The perception on the rigidness of accounting standards seems to be that the respondents believe that I the rules did not allow for flexibility or loopholes then creative accounting would not be so prevalent today. The author would also like to interject here that if measures were rigid, there would also be no need for the constant updating and improving standards. For example, to combat some of the creative accounting practices, measures such as the FRS1 cash flow and FRS2 accounting for subsidiary which opens for more transparent communication between involved parties (Yadav, 2014)

Figure 8: General methods that may be used to curb the use of creative accounting, a perspective from financial statements.



Source: Prepared by the author

From the graph we see that 31% indicated that teaching accounting ethics to accountants and scholars may help to curb the practice, 30% said that improvement of internal audits, while 25% expressed that effective enforcement of accounting laws and policies is their preferred option and lastly the redo of external review did not score well with 14%. From the data gathered, the author assumes the reason why teaching accounting ethics got such high responses, was because of the scholars and students if the learning starts from an early stage in student's studies or career it might foster good ethical practices and also reduce the pressure from managers on accountants to manipulate numbers.

The loopholes in creative accounting are due to the framework of accounting standards allowing these loopholes to be present. All of the significant accounting standards involved top management and some of the biggest accounting firms. In a recent article on Monday 9th April 2018 titled "World's big four accounting firms face £10m fines for serious breaches," stated that the Financial Reporting Council is said to be cracking down on Pricewaterhouse Coopers, KPMG, Ernest & Young and Deloitte for poor audit work (Jones H. , 2018), if this significant accounting and auditing firms are assisting businesses with creative accounting, the practice of creative accounting will continue.

CONCLUSION

Creative accounting has had its fair share of attention in the accounting and finance world. Within recent years we have seen cases where companies are being fined for the practice of creative accounting. The actual idea being the reason for creative accounting is the taking advantage of financial events to protect the specified interest.

The objective of this paper was to examine and discuss how the users of financial statements and induvial in the financial world perceive creative accounting practices to an accounting ethical behaviour point of view. To successfully attain the information, the author began the paper by researching and presenting an extensive theoretical background of the subject by first determining the definition of the creative accounting and also by presenting literature reviews and real-life examples of creative accounting being practised and the outcome of it. In the methodical part of this paper, a series of research questions were formulated and distributed to targeted professional who use, needs or may encounter the financial statement for information.

Having the accounting ethics is very crucial to the credibility of both the accounting and auditing firms, and also of companies, the users of financial statements and accounting information should be dependent on the information provided by accountants. In accounting, ethics is fundamental to show the value and creditability of an organisation.

Based on this study accounting student and scholars require more experience in the understanding of accounting ethics and ethics of manipulation of financial statements. From a theoretical statement mentioned earlier in the paper on whether ethics can be appropriately taught to students, the implementation should still be explored, special training for scholars to be able to teach on the topic also can be introduced, although it is just a start, it might help the train of teaching of the individuals.

Some limitations which the author realized after adding additional information to this paper after the survey had concluded resulted in the author using a secondary source of information. The author realized that he should have added a question relating to the manipulation methods of creating accounting what were discussed in the theory part of this paper. The "What is popular CA manipulation method?" (Bhasin, 2016) , with the options being; off-balance sheet financing, changes in depreciation policy, extraordinary and exceptional items, money valuation and others. The geographical location of this survey was done in India, but the concept may be just as similar in other countries, main aim of the paper was to get opinions from all over the world thus tying the data in perfectly. Also, some of the methods presented are similar to those that were discussed in this paper. From the secondary results the top most responses were in favour that off -balance sheet financing was the most popular mode of creative accounting with 37.65%, making changes to depreciation policy and money valuation were close to each other with 23.52% and 24.70% respectfully. Extra ordinary and exceptional items got a response of 11.78% while others 2.35%. The data coincide with the theoretical chapter of this paper and it also expresses why off-balance sheet financing is seen a s more popular practice, a known example is showed in Table 2. Of this paper, the Enron case.

To make a general consensus, creative accounting will continue to be practiced, despite the continually improving of accounting standards, I believe loopholes will always be found. Nevertheless, attention need to be placed on the ethical aspect of the practice and possible the accounting standards are too opened to interpretation and flexibility.

To answer the research question, "does creative accounting compromise the integrity of accounting ethics," based on the theoretical information and results from the survey conducted, yes it somewhat comprises the integrity of accounting ethics. For one, the accounting ethics are being ignored, the integrity of the data presented will be compromised and those who depend on the data from accounting firms will no long trust these firms. It is also logical that while management may have the notation that they do not have to adhere to the accosting ethical standards, accountants and accounting firms still do and they are the ones who work on behalf of their clients, the mangers, compromising both accounting standards and accounting ethics standards as an accountant.

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APPENDIX

Appendix: Sample Questionnaire

Ethics of Creative Accounting

1. Gender *
Female
Male
Prefer not to say

2. Current geographical location *
North America
Latin, Central America & The Caribbean
South America
Europe
Asia
Other:

3. Profession/ Specialty *
Student (financial/ Accounting)
Accountant
Manager
Other:

4. Do you rely on financial statements to make decisions? *
Yes
No
Sometimes

5. Are you familiar with the term "CREATIVE ACCOUNTING?" *
Yes
No
Maybe

6. The term creative accounting can be interpreted in many ways; it is based on the angle and context in which it is taken. Most commonly, Creative accounting is using the flexibility within accounting to govern the evaluation and the appearance of the accounts so that it will best represent the welfare of the management and their corporations (Jones, Creative Accounting, Fraud and International Accounting Scandals, 2011). Based on the definition, how do you view this practice? *

Good
Bad
Can't say

There are various methods to the process of creative accounting which are expressed in four groups

1. The rules of accounting give way for firms to select a variety of techniques. They are allowed to choose the mode which presents a preferred result or outcome.

2. Within the line of work for accountants a significant level of forecasting, perception and evaluation is present. For instance, when calculating depreciation of an asset, firms usually choose the method which is of more significant advantage to them.

3. Employing the use of fake transactions can change the amounts reported in the balance sheet and may also move profits between accounting periods. This method can be achieved by including more than one deals and with a third party being involved.

4. Business negotiations can be timed base on the corporation decision, this way an image is formulated to express it favors the accounts. (Sakkal)

Methods of creative accounting;

• Increase Income (incomplete sales recognition) • Decrease Expenses (provisions accounting, capitalisation of interest)
• Increase Assets (increase goodwill, revalue fixed assets)• Decrease Liabilities (off-balance sheet financing, reclassifying debt as equity)

7. From your perspective how would you classify this practice of creative accounting? *
Legal
Totally Legal
Don't know
Totally illegal
Illegal

8. If you do, for what do you use financial statements? *
Investment decisions
Lending decisions
Operational decisions
Performance decisions
Other:

9. Who do you believe manipulates Financial Statements*
Accountants
Managers
Auditors
CEOs
CFO
Other:

10. If you were a stakeholder or investor in a particular company and you found out the financial statements were manipulated through creative accounting practices. How would you feel? *
Angry
Disappointed
I do not care
Okay if it benefits me

11. Briefly explain your choice in the above question *
Your answer

12. If you were a manager, accountant, of a particular company, would you manipulate financial statements through creative accounting practices? *
Yes
No
Maybe

13. Briefly explain your choice in the above question *
Your answer

14. Scenario: If business failure is on the brink meaning employees will be unemployed, will it then okay to use creative practices? *
Yes
No

Maybe

15. Do you believe there are any situations that may justify using creative accounting? *

16. Do you think accounting standards are too rigid and force creative accounting due to their view of conservatism? *
Yes
No
Maybe

17. Which do you believe would be the best way to reduce creative accounting, in your opinion. Select as many *
Improve internal audit
Redo external audit
Effective enforcement of laws
Teaching ethics of accounting to accountants and business/accounting students
Other:

Thank you for your time!

BACK

SUBMIT