Trendy v podnikání, roč. 6, číslo 4, s. 11-17, 2016.
Business Trends, vol. 6, no. 4, p. 11-17, 2016.

TAMING CREATIVE ACCOUNTING VIA INTERNATIONAL FINANCIAL REPORTING STANDARDS: THE NIGERIAN SCENARIO

Godsday Edesiri Okoro[1], Emmanuel Ikechukwu Okoye[2]
[1] Godsday Edesiri Okoro, Department of Accountancy, Faculty of Management Sciences, Nnamdi Azikiwe University, Awka, Nigeria, edesirioracle@yahoo.com
[2] Professor Emmanuel Ikechukwu Okoye, Department of Accountancy, Faculty of Management Sciences, Nnamdi Azikiwe University, Awka, Nigeria, eik.okoye@unizik.edu.ng

Abstract: Creative accounting has remained a contentious issue, raising series of arguments in the accounting literature. These arguments are premised on twofold: positive creative accounting (ethical) and negative creative accounting (unethical). Positive creative accounting is grounded on 'fair' accounting practices while negative creative accounting is built on 'inappropriate' accounting practices that may be mendacious to users of accounting numbers. Creative accounting is a way of ethically assisting firms out of the compass of crashing out of business but rather it has been seen as an instrument of destruction. However, this paper examined international financial reporting standards (IFRSs) as a way of taming creative accounting as well as factors that trigger unethical accounting practices in Nigeria. The paper utilized structured questionnaires administered to 120 professionals (auditors, investors, stockbrokers). The Pearson Product Moment Correlation statistical tool was used in analyzing the field data. Based on the analysis, we found that IFRSs can be used to tame creative accounting. This implies that IFRSs moderate excessive unethical accounting practices. We found that one of the most significant factors triggering negative creative accounting is 'conflict of interest'. On the basis of the findings, we recommended that ethical standards by the accounting profession should be properly aligned to suit the present business environment and sustained so as to checkmate excessive use of creative accounting. Also, IFRSs should be fully implemented by all corporate firms as well as more ethical standards that may guide management on creative accounting should be made available by regulatory framework of accounting so as to guide its use without it being detrimental to stakeholders.

Keywords: Creative Accounting; International Financial Reporting Standards; Income Smoothing; Cosmetic Accounting; Accounting Numbers

JEL Classification: M41

INTRODUCTION

The tweaking of accounting numbers by company's management to get a propitious impression has a long history. This history could be traceable to the works of Anglo-Saxon in 1970s and more recently, Watt & Zimmerman (1990); Healy & Wahlen (1999); Gowthorpe & Amat (2005); Susmus & Demirhan (2013); Fizza & Malik (2015) among others. Presently, creative/tweaking of accounting numbers has remained a contentious issue, raising series of arguments in the accounting literature. These arguments are premised on twofold: positive creative accounting (ethical) and negative creative accounting (unethical). Thus, creative accounting may be justified based on the premise of right/wrong accounting practices employed by management of corporate firms. First, positive creative accounting is grounded on 'fair' accounting practices in a bid to tweak accounting numbers; second, negative creative accounting is built on 'inappropriate' accounting practices that may be misleading or mendacious to users of accounting numbers. However, due to unsound accounting practices employed by management of corporate firms (resulting to negative creative accounting), the concept has become an issue of discrepancy

rather than a way of ethically assisting firms out of the compass of crashing out of business.

Fizza & Malik (2015) opined that it is problematic to discern between creative accounting and fraud. The view of Fizza & Malik (op.cit) is further reinforced in the corporate scandals involving Enron, WorldCom, Xerox and in Nigeria, African Petroleum Development, Afribank Nigeria Plc., Oceanic Bank Nigeria Plc. among others. It is near impossible to repudiate the importance of ethics in creative accounting. In order to sustain a sound or fair accounting practices which may be deemed ethical by stakeholders, accounting regulatory body saw the need to initiate the International Financial Reporting Standards (IFRSs) which came as a quick fix to financial reporting by ensuring that fair accounting practices are practiced by corporate firms in their preparation and presentation of financial statements. Thus, the objective of this paper is not only to examine the place of IFRSs in taming creative accounting but also to ascertain the factors triggering unethical creative accounting practices in Nigeria.

1. REVIEW OF RELATED LITERATURE

1.1 What is Creative Accounting?

Creative, aggressive, engineering, decorating, face-beauty, cosmetic accounting, tweaking of accounting numbers, income smoothing and earnings management has been given considerable attention in the accounting literature. Inspite of this, the concept still remains a contentious issue subject to further scrutiny and debate. Creative accounting is a kind of deliberate act perpetuated by management through the utilization of loopholes in accounting regulations for slashing profit variation in order to make financial statements look appealing to users of financial statements. Naser (1993) sees creative accounting as a method of manipulating accounting numbers in a manner whereby accounting professionals utilize the loopholes in the accounting regulations which help them change accounting numbers from their 'real state' to a 'faked state'. Mulford & Comiskey (2002) views creative accounting as financial reporting tricks employed by most corporate firms to moderate their financial statements such that the market value of the company's share increases so as to further encourage investors buy the shares. For instance, corporate organizations by regulations are permitted to select the policy of writing-off research and development expenditures as they occur and payback in the life of related project. However, exploring this accounting loophole gives corporate organizations the chance of faking transactions to alter statement of financial position by a way of showing higher profit in the separate time periods.

Creative accounting is a way of reducing profit or income stream variability at the discretion of company directors (Riedl & Suraj, 2010; Nejad, Zeynali & Alavi, 2013). Siti, Haron & Henny (2013) asserted that creative accounting assists corporate firm moderate year-to-year variations in profits by transferring profits from peak years to less successful years, making organization's profits variation less unstable. Creative accounting as noted by Tokuga & Saki (2011), is a method employed by company's management to reduce infrequent vagaries in income via the application of loopholes in accounting principles.

1.2 The Concept of International Financial Reporting Standards (IFRSs)

In the past, there were country-to-country accounting standards for the preparation and presentation of financial statements. However, due to globalization, accounting regulators and other stakeholders saw the need to have a unified accounting standards, hence the 'International Financial Reporting Standards' (IFRSs). Jeroh & Okoro (2016) observed that prior to IFRSs adoption in 2012 in Nigeria, Statements of Accounting Standards (SAS) was utilized by the Nigerian Accounting Standards Board (NASB) which is presently referred to as the Financial Reporting Council of Nigeria (FRC). IFRSs has now become a framework used by most countries of the world and it is taking a giant stride in Nigeria. IFRSs is a set of harmonized standards and conventions in accounting that make financial reporting uniform, comparable and reliable.

According to Okoro (2013), IFRSs have the likelihood of facilitating cross-country comparability, boost reporting transparency and assisting stakeholders to understand the financial results of entities in a global setting. IFRSs bridges the lacuna in the reporting process of corporate entities which may have been utilized by company management to tweak accounting numbers. IFRSs addresses the concepts underlying the information presented in the general purpose financial statements as well as a basis for judging or resolving accounting issues such as creative accounting. Thus, IFRSs came as a quick fix to financial reporting by ensuring that fair accounting practices are practiced by professional accountants and management.

1.3 Theoretical Framework

This paper is anchored on the 'Agency Theory'. The agency theory holds that conflict may arose between the principal (shareholders) and their agents (managers). Yadav (2014) opined that creative accounting practices may arise due to agency problem. Thus, agency problems is an alternative reasons of crossing the confines of laws or regulations in accounting practices. The theory relies on the contention that managers occasionally pursue their own intents to the detriment of shareholders. The intents that may be pursued by managers could be that of ensuring shareholders wealth is maximized irrespective of whether they engage in unethical or sharp practices (creative accounting) that may make shareholders see the firm beautiful. What is peculiar to managers is that the effective utilization of wealth must be clearly reflected in the financial statements. Ellisabeta & Beattrice (2010) believed that agency theory is connected with creative accounting, as there may be conflict of interest between the users of accounting information. However, IFRSs ensure that no users of financial statement is favoured and all information reported therein should be of interest to all users of accounting information.

1.4 Prior Studies on Creative Accounting & IFRSs

Much has been researched on creative accounting but there are scanty empirical evidences on the relationship between creative accounting and international financial reporting standards (IFRSs) in Nigeria and the world over. Most studies in this area were conducted in developed countries who have fully embraced IFRSs long before it was implemented in developing countries like Nigeria. The study by Fizza & Malik (2015) which scrutinizes creative accounting and financial reporting via structured questionnaires found that creative accounting negatively affects financial reporting. The negative influence is caused by the role played by corporate governance in financial reporting. They believed that creative accounting destroys the image of the company. Kiani & Malik (2015) explored creative accounting in a bid to differentiate earnings management and fraud. They showed that earnings management is done within the regulatory requirements while fraud is done outside the regulatory requirements. Their findings showed that banks, auditors, investors, regulatory authorities, corporate governance are involved in creative accounting.

The theoretical study by Susmus & Demirhan (2013) suggests that GAAP and IAS came into being in order to guide financial accounting activities, although it is impossible to discourage manipulative behaviour of preparers of financial statements, thereby leading to unethical creative accounting practices precipitated by auditors and management of corporate firms. Amat (2013) investigated the nature and prevalence of creative accounting within the milieu of ethical considerations. The study showed that creative accounting is ethically questionable to the professional accountant however, the ethical dilemma militating against the professional accountant encompasses conflict of interest, client proposals to maneuver financial statements and client proposals for tax evasion. Nejad, Zeynali & Alavi (2013) study on income smoothing in Tehran Stock Exchange using Index Eckel supported the position that accounting is one of the method corporate firms adopt in manipulating financial statements. They investigated creative accounting on three levels of profits: net, gross and operating profits and

found that creative accounting is reflected on three levels of profit.

Velury & Kane (2012) examined whether corporate firms experiencing excessive earnings variations are more likely than other firms to report income-decreasing special items as well as if these charges for special items are indicative of creative accounting. The study used regression technique and analysis revealed that firms that are bigger, more in debt and undergoing losses are susceptible to report special items. This suggests that special items charges do not constantly replicate creative accounting but when such manipulative behaviour exists, it may be context-specific, IFRSs has a special role in this regards on special items charges in financial statements that may impinge profits at all levels (gross, operating and net). Tokuga & Sakai (2011) asserted that corporate firms often attempt to regulate instabilities in reported earnings and steer them to levels they deem suitable. They achieve this either by managing reported figures to upturn earnings or to cutback earnings. This according to them, leads to two types of creative accounting behaviour: technical accounting policy (attaining management aim via altering of accounting policies or estimates) and real discretion (attaining management aim via the settlement of accounts by altering contracts or transactions between the firm and its stakeholders). There are provisions preserved in the unified accounting standards (IFRSs) that defines the basis for changing accounting policies or estimates as well as contracts.

The question as to whether the provisions of IFRSs make it possible to moderate excessive unethical accounting practices is still a matter of concern. Our candid believe is that creative accounting offers corporate firm a short-term advantage, however, tweaking of accounting numbers arises when preparers of financial statements take advantage of the gaps in the accounting regulations. The empirical review suggests that there are no empirical evidence on creative accounting and the international financial reporting standards in Nigeria. Thus, our study is one of the first in Nigeria that critically and quantitatively investigates whether international financial reporting standards can tame creative accounting. Furthermore, the review of literatures (conceptual and empirical) enabled us develop the following hypotheses and research questions:

Hypotheses

Ho1: Creative accounting is not significantly affected by international financial reporting standards.

Ho2: Unethical creative accounting practices is triggered by conflict of interest, client proposals to maneuver financial statements and tax evasion.

Research Questions

1. How has creative accounting affected by international financial reporting standards?
2. What is the most significant factor that triggers unethical creative accounting practices?

2. METHODS

This paper adopted a survey design via the administration of primary data (questionnaire). Primary data was gathered through structured questionnaire administered to 120 professionals comprising of external auditors, investors, stockbrokers. The judgmental sampling technique was employed in selecting the respondents for the study. The questionnaire items were developed with 4-point scale rating (1=Strongly Agree, 2=Agree, 3=Disagree and 4=Strongly Disagree). The internal consistency (reliability test) was established using Cronbach Alpha. The instrument yielded a Cronbach Alpha of 0.76. Pearson Product Moment Correlation (PPMC) statistical technique was used in finding out the relationship between creative accounting and IFRSs. Furthermore, descriptive statistics was used to find out the percentage and frequency counts of the respondents. The analysis was performed via the Statistical Package for Social Sciences (SPSS 21.0 version).

3. RESULTS AND DISCUSSION

The paper utilized both descriptive and inferential statistics to find out whether IFRSs

tames creative accounting. First, the descriptive statistics was used to find out the percentage responses against the research questions; second, the inferential statistics was used to validate the research hypotheses. The results are presented in table(s) 1-4.

Tab. 1: Descriptive Statistics: Creative Accounting & IFRSs

Responses	Frequency	Percent	Cumulative Percent
Strongly Agree	59	49.2%	49.2%
Agree	34	28.3%	77.5%
Disagree	19	15.8%	93.3%
Strongly Disagree	8	6.7%	100%
Total	**120**	**100%**	

Source: Field Survey, 2016

Table 1 above show the views of the respondents as to the extent to which creative accounting is affected by IFRSs. From the table above, it reveals that 59(49.2%) and 34(28.3%) of the respondents strongly agree and agree that creative accounting is affected by IFRSs while 19(15.8%) and 8(6.75) disagree and strongly disagree on the question raised above.

Tab. 2: Descriptive Statistics: Factors Triggering Unethical Accounting Practices

Responses	Frequency	Percent	Cumulative Percent
Conflict of Interest	74	61.6%	61.6%
Clients proposal to maneuver	17	14.2%	75.8%
Proposal on tax evasion	22	18.3%	94.1%
Others	7	5.9%	100%
Total	**120**	**100%**	

Source: Field Survey, 2016

Table 2 above show the views of the respondents as regards the factors triggering unethical accounting practices. From the table above, it reveals that 74(61.6%) of the respondents opined that the most significant factor triggering unethical accounting practices is that of conflict of interest which may subsists between managers and stakeholders, followed by proposal on tax evasion 22(18.3%) and clients proposal to maneuver financial statements 17(14.2%). However, respondents identified others factors triggering unethical accounting practices to include non-professional attitude (i.e. lack of knowledge and awareness) and unethical behaviours (immorality and injustice).

Tab. 3: Inferential Statistics: Creative Accounting and IFRSs

	Unstandardized Coefficients		**Standardized**	***t***	**Sig.**
	B	**Std. Error**	**Coefficients Beta**	**B**	
Constant	4.8246	0.3287		15.4151	.000
IFRS	0.4678	0.1439	0.4163	8.9530	.006

Dependent Variable: Creative Accounting

Source: SPSS Output, 2016

Table 3 above shows the inferential statistics between creative accounting and IFRSs. The results showed that IFRSs is positively correlated with creative accounting (P=.006<.0.05), thus the relationship was found significant. This implies that IFRSs can be used to tame creative accounting. However, the standardized coefficient beta (0.4163) shows a positive interaction between the dependent and independent variables.

Tab. 4: Inferential Statistics: Factors Triggering Creative Accounting

	Unstandardized Coefficients		Standardized	*t*	Sig.
	B	Std. Error	Coefficients Beta	B	
Constant	3.1458	0.4253		7.7585	.000
IFRS	0.3077	0.1113	0.3140	3.9001	.005

Dependent Variable: Creative Accounting

Source: SPSS Output, 2016

Table 4 above shows the inferential statistics of the factors triggering creative accounting. The results showed that the overall factors (i.e. conflict of interest, proposal on tax evasion, clients proposal to maneuver financial statements, non-professional attitude and unethical behaviours jointly triggers unethical creative accounting. Thus, these factors *inter-alia* are correlated with creative accounting ($P=.005<0.05$), thus the relationship was not flawed. This result suggests that these factors *inter-alia* triggers unethical creative accounting. The above result is further supported by the standardized coefficient beta of 0.3140.

CONCLUDING REMARKS

This study investigated the place of the international financial reporting standards (IFRSs) in taming creative accounting. The empirical results suggest that IFRSs essentially tames creative accounting such that is helps to moderate excessive unethical accounting practices that may lead to manipulating of financial statements. This implies that IFRSs moderate excessive unethical accounting practices by corporate organizations. In addition, we found that one of the major factors triggering negative (unethical) creative accounting is that of conflict of interest between principals and owners of wealth. There also factors triggering negative creative accounting such as client proposals to maneuver financial statements and proposals on tax evasion. Because firms want to evade tax, they may report unrealistic profit. On the basis of the findings, we recommended that ethical standards by the accounting profession should be properly aligned to suit the present business environment and sustained so as to checkmate excessive use of creative accounting. Also, IFRSs should be fully implemented by all corporate firms as well as more ethical standards that may guide management on the use of creative accounting should be made available as a matter of urgency by accounting regulatory framework. This becomes paramount so that such creative accounting guidelines will guide its usage without it being detrimental to stakeholders.

REFERENCES

Amat, O. (2013). Creative accounting: Nature, incidence and ethical issues. *Journal of Economic Literature*, 1(1), 1-19.

Ellisabeta, B.D. & Beattrice V.A. (2010). Creative accounting: Players and their gains and losses. *Annals of Faculty of Economics*, 1(2), 813-819

Fizza, T. & Malik, Q.A. (2015). Creative accounting and financial reporting: Model development and empirical testing. International *Journal of Economics and Financial Issues*, 5(2), 544-551

Gowthorpe, C. & Amat, S.O. (2005). Creative accounting: Some ethical issues of macro and micro-manipulation. *Journal of Business Ethics*, 57, 55-64

Healy, P.M. & Wahlen, J.M. (1999). A review of the creative accounting literature and its implications for standard setting. *Accounting Horizons*, 13(4), 365-383

Jeroh, E. & Okoro, G.E. (2016). Evaluating the effect of IFRS adoption on the financial position of commercial banks in Nigeria. *Scientific Papers of the University of Pardubice, Faculty of Economics and Administration, Series D*, XXII (36), 130-140

Kiani, D.S. & Malik, Q.A. (2015). Creative accounting: Developing a model. Research *Journal of Recent Sciences*, 4(11), 146-150

Mulford, C.W. & Comiskey, E.E. (2002). *The financial numbers game: Detecting creative*

accounting practices. Canada: John Wiley & Sons. Inc.

Naser, K. (1993). *Creative financial accounting: Its nature and use. Hemel* Hempstead: Prentice Hall.

Nejad, H.S. Zeynali, S. & Alavi, S.S. (2013). Investigation of income smoothing at the companies listed on the Stock Exchange by the using of Index Eckel: A case study of Tehran Stock Exchange. *Asian Journal of Management Sciences and Education*, 2(2), 49-62

Okoro, G.E. (2013). Accounting profession and IFRS adoption in Nigeria: Benefits and demerits connected with IFRSs implementation. *Journal of Social and Management Sciences, Special Edition*, pp.68-70

Riedl, E. & Suraj, S. (2010). Signaling firm performance through financial statement presentation: Special items. *Contemporary Accounting Research*, 27(1), 289.

Siti, M.S., Haron, R. & Henny, H.M.T. (2013). Income smoothing and Islam: An evidence from Malaysian Shariah compliant companies. *International Journal of Social Science and Humanity*, 3(2), 160-162

Susmus, T. & Demirhan, D. (2013). Creative accounting: A brief history and conceptual framework. *Journal of Akademik Bakis Bergisi*, 38(1), 1-20

Tokuga, Y. & Saki, A. (2011). Income smoothing as a form of accounting policy by managers: A case study of Onward Kashiyama. *Working Paper*, pp.1-24

Velury, U. & Kane, G. (2012). Big bath, income smoothing, and special items: An empirical investigation. *Public and Municipal Finance*, 1(1), 80-86

Watt, R.L. & Zimmerman, J.L. (1990). Positive accounting theory: A ten year perspective. *Accounting Review*, 65(1), 131-156

Yadav, B. (2013). Creative accounting: A literature review. The SIJ Transactions on Industrial, *Financial and Business Management,* 1(5), 181-193.