

ACCOUNTING POLITICS IN CONTEXT OF ANNUAL ACCOUNTS

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Abstract: *Today, world accounting is undergoing a great reconciliation process, mostly determined by the globalization phenomena of financial markets and economy. Romanian accountancy couldn't remain indifferent to the challenges that word accounting is facing due to accentuation of globalization phenomena. Romania made no exception when its economy was globalised and aligned with the European one. The period after December 1989 we witnessed two phases of the Romanian accounting system reform. The first phase was a slow one, but with spasms due to conflict between generations: innovators and conservators, pro-west and nostalgic of “the socialist society multilateral developed”, pro-continental and pro-Anglo-Saxons.*

Free of storms and fine weather, this first stage perfectly benefited of French expertise, successfully fitted on the general accounting plan borrowed from the Romanian Bolshevik period, and the progress of western systems, which a country like France had to have them. During the second phase of reform, attention is manifested in assuring that the Romanian accounting system is comparable with evolutions that occur in accounting worldwide. An accounting system based on International Standards of Financial Statements is implemented. In a framework in which the leu is agonizing we prefer to swap, we swap Bordeaux wine with Glasgow whisky. The British expert replaces the French one. The presence of European component in Romanian accounting is a commitment that our country made when signing the European accounting guidelines. Let's not forget that Romania wants to enter fully righted the European Union. The presence of international components in Romanian accounting is beneficent.

Few are the accounting managers that understand the accounting reconciliation and the assimilation of IAS as simple changes in the account plan and changes in the balance sheet and profit and loss account. Of course, such a perception and understanding the reconciliation steps of Romanian accounting system is completely inefficient. Virtually conceptual changes are being made and have to be done, another way of approaching the process of conceiving, designing and elaborating accounting information, orientated and assigned for a wide variety of users through summarized financial statements.

Before 24/2001, accounting politics have been requested in an appendix, the last of the balance sheet, named “Other information regarding rules and accounting methods and additional data”. These were either briefly presented or not at all. When the Romanian accounting reconciliation program with Directive IV of the CEE and International financial reporting standards, was launched developing enterprise accounting politics becomes the most important.

Based on IAS rule no 1, accounting politics are the steps of an enterprise made to adopt principles, bases, conventions, rules and specific practices adopted by a company to draw and present financial statements. From another point of view, accounting politics are the choices made by managers to shape in a licit framework the presentation and content of financial statements.

The Dictionary of accounting from Oxford University Press defines accounting politics as being “specific accounting bases and permanently used by an organization as being the most adequate to present precisely its financial results and operations...”¹

¹ *Dictionary of Accounting*, Edited by R.Hussey, Oxford University Press, Second Edition, 1999

A more colorful definition belongs to Christopher Nobes: “accounting politics are detailed methods to evaluate, to measure and recognize (to determine) which an enterprise chose from the ones general accepted by the law, accounting standards or commercial practices”².

In the context of the legal reconciliation program of Romanian accounting system, elaborating and underlying company accounting politics has to circumscribe the spirit, principles and requirements of the European accounting directives and International standards of financial reporting.

In Romanian accounting regulations, the financial statement intended for accounting politics is found as “Accounting principles, politics and methods”. It presents:

- deviations from accounting principles and the change of evaluation methods;
- alternative accounting treatments;
- the amount of interest included in the production cost of frozen and current assets with a long production cycle.

According to the Directive to modify and add up the Accounting law no. 82/1991 published in the O.M. of august 24 2004, art.26 specifies that “accounting politics used to draw annual financial statements have to be according to applied accounting regulations”.

International standards of financial reporting bring out professional reasoning. Professional reasoning is the one that underlay accounting and financial politics of the company (starting from useful economic life and depreciation methods of frozen assets to evaluation methods in the balance sheet of different reported elements). In some situations International standards of financial reporting allow two accounting approaches for transactions and events of the same kind (base accounting approach and alternative allowed accounting approach).

In the situation in which a base approach and an alternative one allowed to solve the same problem are given, accounting politics are elaborated and settled in the context of free choice between the two methods, to establish and draw up information regarding the company’s financial position and flow of money. When a certain accounting politic will be chosen, the impact this would have upon the company’s financial position and performances will be taken into consideration. For example, opting to deduct grant from the asset’s price will lead to the diminution of depreciation, thus influencing the total of the balance sheet and the result of the company. Choosing short periods of depreciation will lead to higher depreciation costs, which will influence the company performance. Defining enterprise accounting politics has obvious consequences upon determining the proportion of the result, which becomes variable according to the interest sought after. Actually in determining the result subjectivism occurs. The result can not be looked as a plain difference between incomes and expenses it is an endogenous datum, a result of management decisions. One can say that the size of the result becomes a strategic decision, its level being settled by managers through accounting politics.

Many times, following management objectives of the company leaders, the accountant will be tempted to choose subjectively:

-to diminish the result:

- extracting expenses with risks provisions and depreciations;
- extracting general expenses;
- sub evaluating stocks;

-to increase the result:

- abandoning claims inside a group
- incorporating financial expenses in the acquisition cost of frozen asset or stock;

Economic theory considers that the object of any enterprise is the maximization of profit. However, there are companies that wish to obtain a satisfactory profit. Accounting practices allow enterprises to present to some extent results according rather to their objectives than reality. Some

² Nobes C., *Pocket Accounting, The Economist Books*, 1999 quoted after N. Feleaga, L. Malcui, *Accounting politics and options*, Economic Press, Bucharest, 2002, pg 13.

of these practices, named accounting politics, are a result of choosing between different accounting methods and lead to the improvement of current result and net result, or to the alteration of the result structure without tampering with the net result.³ Although financial information is made in a legal environment which regulates in a rather precise manner its presenting rules, we usually discover that a correction of the result is being made by many companies and the balance sheet is adjusted which is legal and rightful, thus they profit from the permissive legal and accounting rules, this is why it is called creative accounting.

The concept of “creative accounting” is mostly found in British and French writings. Jan Griffiths writing from the perspective of a business journalist observes: “Every company in the country is fiddling its profits. Every set of published company is based on books which have been gently cooked or completely roasted. The figures which are fed twice a year to the investing public have all been changed in order to protect the guilty. It is the biggest con trick since the Trojan horse....In fact this deception is all in perfectly good taste. It is totally legitimate. It is creative accounting.”⁴ Michael Jameson, writing from the perspective of accountant, argues: “The accounting process consists of dealing with many matters of judgment and of resolving conflicts between competing approaches to the presentation or the results of financial events and transactions....this flexibility provides opportunities for manipulation, deceit and misrepresentation. These activities- practiced by the less scrupulous elements of the accounting profession- have come to the known as creative accounting”.⁵

Kamal Nasser, presenting an academic view, offers this definition: “Creative accounting is the transformation of financial accounting figures from what they actually are to what preparers desire by taking advantage of the existing rules and/or ignoring some or all of them”.⁶ Creative accounting refers to accounting practices that derive from standard accounting practices. They are defined by excessive complications and creativity similar to that of writing a novel, its goal is to favorably present a company’s financial position and performances. Financial statements obtained by this technology “are not at all boring”, but have the complexity of a novel, therefore the name of “creative” or “innovating”.

Creative accounting is a complex system of methods its objective being the alteration of the result level in order to optimize or minimize or present financial statements without the exclusion of either one of the two objectives.

Companies that draw financial statements according with new regulations will have to give greater attention to accounting politics as a component of financial statements in order to provide accounting information that has the quality parameters stated in the conceptual accounting content of IASB. The management based upon professional judgment, will have to develop accounting politics that insure the input of information through relevant and credible financial statements.

References

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³ Malciu L., *Creative accounting*, Economic Press, Bucharest, 1999, pg 31

⁴ Griffiths I., *Creative Accounting*, London, Sidgwich & Jackson, 1986, pg 1

⁵ Jameson M., *Practical Guide to Creative Accounting*, London, Kogan Page, pg 7-8

⁶ Naser K., *Creative Financial Accounting: Its Nature and Use*, Hemel Hempstead: Prentice Hall, 1999, pg 2