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The influence of creative accounting on the credibility of accounting reports

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Abstract

Purpose – The extent to which accounting reports and disclosures provide shareholders and other interested parties with reliable information to permit informed investment decisions and true valuation of firms, has remained in doubts. The presumed bane for the failure of these reports to live up to expectation has been creative accounting. Most studies view this practice as unethical and should be stopped; others admit that although it contributes to enterprise failures, loss of investments and economic crisis, it as a necessary and legitimate practice. This paper aims to evaluate the extent to which this creativity has contributed to the failures of enterprises, identifies motivations for this practices and the challenges to true and fair reporting and transparent disclosures.

Design/methodology/approach – The study adopts the survey method. Questionnaire were administered to 80 accountants in banks and other enterprises with parents companies outside Nigeria and secondary data collected on failed enterprises in the world. The data collected were descriptively analysed.

Findings – The findings were different from findings of previous studies. It was discovered that accounting creativity is euphemism and contributes 90% to the unfair reporting of firms operations. The creativity in those practices is motivated by greed and intended to deceive the public, potential investors and shareholders and increases the rate of enterprise failures at a decreasing rate. However, the study revealed that the many regulations without adequate checks, punishments and rewards complement creative accounting in providing the foundation for make-believe, cosmetic and unfair reporting.

Research limitations/implications – The use of questionnaire and the subjective nature of the responses are the limitations of this study.

Practical implications – Improved reporting and valuation of firms are the practical implications.

Social implications – Reduction in failures may result in loss of employment and other social implications.

Originality/value – The research is original and born out of the desire to improve accounting reports and shareholders value.

Keywords Financial reporting, Accounting, Accountability, Fair, Creative, True

Paper type Research paper

1. Introduction

The recent failures of economic enterprises have raised a number of credibility questions about Accounting as a System of authentication and the reliability of its report in reaching optimal management and investment decisions. The collapse of Enron, World.Com, BCCI, Robert Maxwell Pension Funds, Global Crossing, Adelphia, Tyco and the demise of Arthur Andersen, one of the "Big Five" accounting firms are cases on point (Cadbury's Report, 1992;

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Ramly and Rashid, 2010; McColgan, 2001; Khan, 2011; Li and Broshko, 2006; and Heath and Norman, 2004). These cases prove without a doubt that the financial reports presented by the management to public and certified by auditors were a misrepresentation of the true position of the firms. The accountants, management and the auditors are indicted for manipulation, unfair and misrepresentation of facts and figure to achieve pseudo results and the overlooking of such misrepresentation to issue a clean opinion to such management.

Amidst these crises and business failures, and consequent loss of reputation for the accounting profession, many studies have been conducted on this "creative" accounting practices, their manipulations, re-representations and motivations (Beshiru and Izedonmi, 2014, Fizza and Qaisar, 2015). Some blame the incidences of these creative manipulations on the inadequacies of the Generally Acceptable Accounting Principles (GAAP) and ignore or support those who capitalize on the loopholes or inadequacies of GAAP. Others condemn the practices and suggest more regulations to curb the practice. Both ways, the blame is on the system and not on the perpetrators of the act. Some of the perpetrators, in the studies by Naser (1993) and Amat and Blake (1996), are justified that the manipulations of different forms and deceptive re-representation of fact and figures about the operations of an enterprise are legitimate and do not influence the credibility of financial reports. This justification is properly observed by Griffiths (1986, p. 1):

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

Few practitioners are hopeless about the solution to these manipulations, given how deeply rooted the practices are and to whom it benefits the most. Therefore, there is need to ascertain the level of negative influence this creativity exerts in discrediting accounting reports. This research is motivated by the deepening of this decay. It seeks to further the need to understand the motivations for the negative creativity and determine the direction and intensity of actions required in curbing its perpetration and penetration into the economic lives of enterprises and their stewards.

To this end, the study seeks to examine the "creativity" in creative accounting, examine the motives of this creativity and its implications for the enterprise health, ascertain the influence of such benefits in encouraging more negative creativity, find out other complementary variables that encourage facts and figures manipulations and misrepresentations and suggest possible strategies to reduce or control its spread. This study therefore further seeks to examine the influence of creative accounting practices on the rate of enterprise failure across the globe. It seeks to ascertain the extent to which creative accounting practices increases the rate at which enterprises across the globe fails.

This paper is discussed in five sections. The first is the introduction. In Section 2, the theoretical aspects and relevant literature are reviewed. In this section, the concept of creativity and the various definitions and practices of creative accounting are discussed critically. In Section 3, the methodology is presented, and in Section 4, the findings are presented and discussed. This section assesses the creativeness or otherwise of the accounting creativity, discusses the influence of this negative creativity in discrediting accounting reports, highlights the consequences of such accounting practices and examines other factors that complements the negative accounting creativity. The conclusion and recommendations are made in Section 5.

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2. The concept of creativity and creative accounting

This section is discussed in two parts. The first part examines creativity as a concept. The second part examines the definitions and forms of creative accounting and the various practices that fall under such definition. It considers the motivation for such practices. This is intended to provide a basis for assessing the creativity and the justification for accounting creativity. The theoretical framework is also given in this section.

2.1 The concept of creativity

More than 60 different definitions of creativity can be found in the psychological literature (Taylor, 1988). The etymological root of the word in English and most other European languages comes from the Latin *creatus*, literally "to have grown". Creativity is a process involving the generation of new ideas or concepts, or new associations between existing ideas or concepts, and their substantiation into a product that has novelty and originality. From a scientific point of view, the products of creative thought (sometimes referred to as divergent thought) are usually considered to have both "originality" and "appropriateness". An alternative, more everyday conception of creativity is that it is simply the act of making something new.

Perhaps, the most widespread conception of creativity in the scholarly literature is that creativity is manifested in the production of a creative work (for example, a new work of art or a scientific hypothesis) that is both "novel" and "useful". Colloquial definitions of creativity are typically descriptive of activity that results in producing or bringing about something partly or wholly new; in investing in an existing object with new properties or characteristics; in imagining new possibilities that were not conceived of before; and in seeing or performing something in a manner different from what was thought possible or normal previously. Creativity is also seen by economists such as Paul Romer as an important element in the recombination of elements to produce new technologies and products and, consequently, economic growth. Creativity leads to increase in capital, and creative products are protected by intellectual property laws. The "creative class" is seen by some to be an important driver of modern economies. In his 2002 book, *The Rise of the Creative Class*, economist Richard Florida popularized the notion that regions with high concentrations of creative professionals such as hi-tech workers, artists, musicians and creative people and a group he describes as "high bohemians", tend to have a higher level of economic development.

In a summary of scientific research into creativity, Mumford (2003, p. 110) suggested: "Over the course of the last decade, however, we seem to have reached a general agreement that creativity involves the production of novel, useful products". Creativity can also be defined "as the process of producing something that is both original and worthwhile" or "characterized by originality and expressiveness, imaginative, increase in capital, results in economic development, add value to the society, and have in the long run positive consequences" (Csikszentmihalyi, 1999, 2000; Runco and Albert, 2010; Runco, 2004; Sternberg and Lubart, 1999). To distinguish clearly the direction of creativity, Pink (2005) argued that we are entering a new age where creativity is becoming increasingly important. In this "conceptual age", we need to foster and encourage "right-directed thinking" (representing creativity and emotion) over "left-directed thinking" (representing logical, analytical thought). Therefore, what is creative must be devoid of deception. The motivations for creativity are in line with the characteristics highlighted above. In simple terms, creativity consists largely of re-arranging what we know to find out what we do not know.

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2.2 Accounting creativity: meaning, forms and practices

The term creative accounting is neither found in any accounting standards or regulations nor the procedures for its practices spelt out. The definitions under consideration are as opined by observers and practitioners. The definitions of creative accounting vary and include the following:

- The deliberate dampening of fluctuations about "some level of earnings considered to be normal for the firm (Barnea *et al.*, 1976).
- Any action on the part of management which affects reported income and which provides no true economic advantage to the organization and may in fact, in the long-term, be detrimental (Merchant and Rockness, 1994).
- A process that involves the repetitive selection of accounting measurement or reporting rules in a particular pattern, the effect of which is to report a stream of income with a smaller variation from trend than would otherwise have appeared (Copeland, 1968).
- The process of manipulating accounting figures by taking advantage of the loopholes in accounting rules and the choices of measurement and disclosure practices in them to transform financial statements from what they should be, to what preparers would prefer to see reported, and the process by which transactions are structured so as to produce the required accounting results rather than reporting transactions in a neutral and consistent way (Naser, 1993 p. 59).
- Schipper (1989) observes that "creative accounting" can be equated with "disclosure management", "in the sense of a purposeful intervention in the financial reporting processes".

This practice has different names and forms in different countries. For more explanations on all the various global nomenclature, we enclose Table I.

Creative accounting is practiced in the different forms and names highlighted in Table I, and the preferred term and consequently in most of the literature on the subject is "earnings management"; but in this paper, the term "creative accounting" will be used. This is because of the recognition that some accounting manipulation involves primarily balance sheet items rather than earnings items.

Country	The equivalent of the Romanian "creative accounting"
Switzerland	Bilanzmanipulation, Bilanzkosmetik ,heisse Luft
Germany	Tricksereien , Bilanzartistik, geschönte Jahresrechnung, Seifenblasen
Holland	Winstegalisatie (profit equalization), Creatief boekhouden, Creatieve jaarverslaggeving, Winststuring (earnings management), Winstflattering, Verliesmaximalisatie
France	Bricolage (DIY), Fabricated accounts, Unlimited creativity
USA	Cooking the books, fabricated numbers, fiddle the numbers, more debits than credits, earnings management
Italy	Politiche di bilancio
Japan	Furyo Kessan (improper accounting); Funshoku (window-dressing), Kara-uri (dummy or "empty sales"); Mae-daoshi (bringing sales forward)
Australia	Fudging, Manipulative accounting, Feral accounting
Great Britain	Window-dressing, Accounting for profits, Bubbles, Enronitis

Source: Audit Committee Newsltter, KPMG, June, 2003

Table I. Global nomenclature and forms of creative accounting

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The techniques that define creative accounting are not new, but experience has shown that most of the times they may prove extremely expensive. To attract investors and to appear profitable to the shareholders, employees, creditors, suppliers and other categories of stakeholders, the companies can decide to misstate the financials. This practice often leads to drastic consequences. These consequences manifest due to six principal areas of weaknesses or loopholes in accounting regulations and practices, namely, regulatory flexibility, a dearth of regulation, a scope for managerial judgment in respect of assumptions about the future, the timing of some transactions, the use of artificial transactions and finally the reclassification and presentation of financial numbers (Largay, 2002; Mulford and Comiskey, 2002; Diana *et al.*, 2014). These areas are discussed in turn:

- *Regulatory flexibility*. Accounting regulation often permits a choice of policy; for example, in respect of asset valuation (International Accounting Standards permit a choice between carrying non-current assets at either revalued amounts or depreciated historical cost). Business entities may, quite validly, change their accounting policies. As Schipper (1989) points out, such changes may be relatively easy to identify in the year of change, but are much less readily discernible thereafter.
- *Dearth of regulation*. Some areas are simply not fully regulated. For example, there are (as yet) very few mandatory requirements in respect of accounting for stock options. In the majority of countries, like Spain for example, accounting regulation in some areas is limited. For example, the recognition and measurement of pension liabilities and certain aspects of accounting for financial instruments.
- *Scope of managerial judgement and estimation on discretionary areas*: Management has considerable scope for estimation in discretionary areas. Management can use their discretionary position in order to obtain the financial position and stability they assumed. For example, the managers can decide the increase or reduce of the provisions for bad debts. McNichols and Wilson (1988), for example, examine the discretionary and nondiscretionary elements of the bad debts provision.
- *The timing of some transaction*: Genuine transactions can also be timed so as to give the desired impression in the accounts. The timing of some transactions offers to the management the opportunity to increase the revenues, when the operating profit is not satisfactory, and to create the desired impression in the accounts. The existing stocks in company's patrimony, that have a significant higher value compared to the historical value, may be sold only when the operating profit is not satisfactory. As an example, suppose a business has an investment at historic cost which can easily be sold for a higher sales price, being the current value. The managers of the business are free to choose in which year they sell the investment and so increase the profit in the accounts.
- *The use of artificial transaction*: Artificial transactions can be entered into, to manipulate balance sheet amounts and to move profits between accounting periods. This is achieved by entering into two or more related transactions with an obliging third party, normally a bank. For example, supposing an arrangement is made to sell an asset to a bank then lease that asset back for the rest of its useful life. The sale price under such a "sale and leaseback" can be pitched above or below the current value of the asset because the difference can be compensated for by increased or reduced rentals.

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- *Reclassification and presentation of financial numbers*: Reclassification and presentation of financial numbers are relatively under-explored in the literature. However, the study by Gramlich *et al.* (2001) suggests that firms may engage in balance sheet manipulation to reclassify liabilities to smooth reported liquidity and leverage ratios. A special type of creative accounting practice relates to the presentation of financial numbers, based on cognitive reference points. As explained by Niskanen and Keloharju (2000), the idea behind this behaviour is that humans may perceive a profit of, say, 301 million as abnormally larger than a profit of 298 million. Their study and others (van Caneghem, 2002) have indicated that some minor massaging of figures do take place to reach significant reference points.

If we explore these definitions and practices, we find that some interesting assertions are implied. By saying that creative accounting transforms accounts from what they 'should' be, it is implied that there is some absolute truth in accounting that could be achieved if only the rules were applied impartially. Similarly, there is a reference to an idea that transactions should be reported in a "neutral and consistent" way. The term neutral again implies a need for impartiality. This position is supported by our survey findings where all respondent (100 per cent) agreed that creative accounting practices distort the true or real accounting results. By implication therefore, it is not the systems of rules that is to blame, but accountants and managers' greed to capitalize on what they see as loopholes and weaknesses to ruin the future of an economy. These operators lack the virtues to support the smooth operations of the rules and thus lack the most important ingredient that defines creativity and accountability (Akpanuko and Asogwa, 2013).

2.3 The theoretical foundations

The theory that explains these motivations is the agency theory. This theory is rooted in the work of modern corporation and private property on the separation of firm ownership from the management and often credited to the landmark work on theory of the firm: managerial behaviour, agency cost and ownership structure (Jenson and Meckling, 1976; Fama and Jensen, 1983; Brijesh, 2014). They suggested that agency problems will always arise in circumstances where the principal (owners, shareholders) employs the agent (board/management) to undertake a number of duties on their behalf for a reward. Thus, the management in acting in the capacity of an agent to the principals owes principals fiduciary duty of care to run the organization in the best interests of the owners for a given reward (Berle and Means, 1932; Jenson and Meckling, 1976). They however argued that conflicts of interest do inevitably exist between the management and the owners of the businesses especially in cases where owners are not managers. This is because the agency theory assumes a model of managers as a man that is self-interest seeking, self-serving, individualistic and optimistic in nature that only prefers to maximize his personal utility functions at the expense of the owners (principals). The theory holds that there exists always a divergence of objectives between the goals of the management and those of the shareholders. Agency problems could also arise due to adverse selections and moral hazards (Jenson and Meckling, 1976). Moral hazard refers to a situation where due to imperfections in the contract between the principal and the agent, the management may take sub-optimal decisions and may be opportunistic (Adelopo, 2010).

While moral hazards tend to happen after the contract, adverse selection may occur both before and after the contract between the principal and the agent (Adelopo, 2010). Adverse selection refers to the possibility of the principals or shareholders hiring agent who do not have the right type and kind of skills that may enable them to deliver the expected returns

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(Adelopo, 2010). This may be due to existence of information asymmetry between parties or inherent imperfections in the contracting process (Gomez-Mejia and Wiseman, 2007). Given that shareholders have risk altitudes that are different compared to management (Jenson and Meckling, 1976), the continuous existence of information asymmetry may compel the principal to impose some forms of controls. These control mechanisms usually require the allocation of resource, while in addition, it tends to increase the cost of operations, often refers to as the agency cost. This explains the occurrence of these practices in these corporations amidst its negative impact and criticisms.

Most commentators view creative accounting with distaste. Wikipedia sarcastically describes accounting creativity as euphemisms. In this line, Griffiths (1986) and Jameson (1988, p. 20) declare, "Let there be no doubt about it, creative accounting is a bad thing. It distorts company results and financial position and, if the theorists are to be believed, its practice is likely to become increasingly common". Smith (1992, p. 9) illustrates his contention that creative accounting is a serious problem with case studies of three UK listed companies, which collapsed shortly after presenting accounts that indicated financial strength. The author argues, "These three large corporate collapses all owe their occurrence in some respects to techniques of creative accounting or financial engineering".

Several studies have been conducted on this subject (Largay, 2002; Mulford and Comiskey, 2002; Csikszentmihalyi, 1999, 2000; Runco and Albert, 2010; Runco, 2004; Sternberg and Lubart, 1999), yet its influence on the accounting reports' of firms has not been ascertained.

3. Research methodology

This study adopts a survey/descriptive and analytical research design. The aim is to extensively review related literature, collect primary data from practitioners, draw inferences on the subject via descriptive statistical analysis of multinational firms in Nigeria and assess the global influence of these practices on accounting report falsification and failure of enterprises. Eighty accountants were strategically selected for this study from different Multinational business enterprises in Nigeria. The sample size of 80 professional accountants in these enterprises was judgementally based on their agreement to participate in the study. Structured questionnaire is used for data collection with simple closed ended, multiple choice and open-ended questions on the subject of study. The data collected are tabulated and analysed using descriptive statistics. The data obtained are used in the validation of the research questions. The hypothesis is tested using secondary data. The number of failed enterprises and the rate of failures that are reported across the globe is used as the dependent variable. The proportion of creative accounting factors to total factors contributing to a firms' failure will be used as independent variable in testing the hypothesis. The research hypothesis is validated using regression and correlation analysis. The model is $CF = a + b_1CAP + e$. Where CF is Corporate Failures, CAP is Creative Accounting Practices, b_1 is the coefficient and e is the error factor.

4. Data analysis and discussion of findings

The respondents returned all the questionnaires in useable form. Among the respondents, 42 per cent were female and 58 per cent were male, and all had the Accounting Professional qualification. In total, 83.5 per cent of the respondents had over 20 years of reporting experience, while 16.5 per cent had less than 20 years reporting experience. The demographics of the respondent reveal their wealth of experience and expertise in the area of study. The responses obtained are organized to address the research objectives.

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4.1 Is creative accounting a major ethical challenge?

The study reveals that creative accounting is a major ethical problem even in Nigeria. This is corroborated by the responses where 61 per cent of respondents stated that the problems of manipulation of financial information by clients, presented an ethical problem for accounting professionals in Nigeria (Table II). This in line with a study carried out by Leung and Cooper (1995) on 1,500 accountants in Australia.

4.2 How creative are these practices?

In answering this question, we compare the qualities, characteristics and motivations of creativity with the concept of creativity as applied in accounting. We consider first the motivations, second the originality, third the unknown expectation and finally the positive economic consequences.

First, various studies have examined the issue of management motivation towards creative accounting behaviour. The motivation for accounting creativity is negative and borne out of selfish interest of managers to deceive shareholders and the investing public that all is well or will be well when actually none maybe well. Hepworth (1953), Beidleman (1973), Healy and Wahlen (1999), Fox (1997) and Trueman and Titman (1988) identified several motivations for creative accounting including:

- Tax reduction
- Deceptive boosting of confidence of shareholders and investors by reporting stable earnings and psychological expectations relating to increases in anticipated income. Another form of deception in this direction is called "big bath" accounting, where a company making a bad loss seeks to maximize the reported loss in that year so that future years will appear better.
- Income smoothing on expectations, securities valuation and some element of risk reduction for analysts. A variant on income smoothing is to manipulate profit to tie in to forecasts. Fox (1997) reports on how accounting policies in some companies are designed, within the normal accounting rules, to match reported earnings to profit forecasts. When these companies sell products a large part of the profit is deferred to future years to cover potential upgrade and customer support costs. This perfectly respectable, and highly conservative, accounting policy means that future earnings are easy to predict. Company directors may keep an income-boosting accounting policy change in hand to distract attention from unwelcome news. Collingwood (1991) reports on how a change in accounting method boosted a company's quarterly profit figure, by a happy coincidence distracting attention from the company slipping back from being the largest company in the industry in the USA to the number two slot.

Options	No. of respondents	(%)
Conflict of interest	13	19
Client proposal to manipulate accounts	51	61
Client proposal for tax evasion	16	20
Total	80	100

Note: Field survey (2015)

Table II. Most frequent ethical problems in Nigerian enterprises

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- To provide a boost when significant capital market transactions are anticipated, and when there is a gap between the actual performance of the firm and analysts' expectations and to reduce the perception of variability in underlying economic earnings of the firm. This helps maintain or boost the share price by reducing the apparent levels of borrowing, so making the company appear subject to less risk, and creating the appearance of a good profit trend. This helps the company, a non-performing firm, to raise capital from new share issues, offer their own shares in takeover bids, and resist takeover by other companies. If the directors engage in "insider dealing" in their company's shares they can use creative accounting to delay the release of information for the market, thereby enhancing their opportunity to benefit from inside knowledge.
- Another set of reasons for creative accounting, which applies to all companies, arises because companies are subject to various forms of contractual rights, obligations and constraints based on the amounts reported in the accounts.

Second, the outcome of the accountants' creativity is not original, but a manipulation of an existing figure (the true and fair state) to produce an expected outcome (the false state). Third, the expected state is a known outcome which is contrary to the defining characteristics of creativity. Finally, the consequences of creative accounting in the long run are negative economic events that can transcend continents. The 2007 economic crisis was a case in point. Thus, creative accounting is best described as euphemism created out of managements' and accountants' greed at the detriment of the economy. It is unethical practices made legitimate on purpose and not due to ignorance or absence or inadequacy of rules and regulation. The accountant deceptively creates financial statement to suit the required deceptive purpose using different strategies. The responses are as contained in Table III. Table III provides a summary of the strategies adopted in Nigerian companies.

From the survey, the following nine strategies were identified. These strategies are fallout of the major practices listed in Section 2.2. The statistic shows the depth of these deceptive practices.

4.3 The influence of this negative creativity in discrediting accounting reports

The existence and deepening of these practices with the given level of legitimacy has encouraged even more negative creativity and more will be invented no matter the level of regulation. Schiff (1993, pp. 94-95) identifies other six common strategies used by the accountants in companies to re-represents firms' operations:

Table III. Strategies of creative (deceptive) accounting

Strategies	No. of respondents	(%)
Over valuation of closing stock	56	70.0
Ignoring provisions for bad debt/legal obligations	40	50.0
Sales purchase back	20	25.0
Playing with debit and credit	67	84.0
Big bath charges	78	98.0
Creative acquisition accounting	12	15.0
Cookie jar reserves	45	56.0
Materiality	68	83.7
Revenue recognition	55	69.0

Note: Field survey (2015)

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(1) hiding of the pension liabilities;
(2) capitalizing the expenses instead of writing them off;
(3) realizing and increasing of the receivables or inventories versus sales;
(4) negative cash flow;
(5) consolidating the affiliates' incomes and net worth; and
(6) following seemingly conservative practice in a situation of reverse direction.

For instance, using last in first out when or where first-in first-out method of valuation would have been appropriate. These actions are taken with a clear knowledge of the effects and consequences. This fact was attested to by 83 per cent of the respondents in the survey.

Globally, the number of failed enterprises is increasing. The author has tabulated the number of firms that had failed and their year of failure. This is shown in Table IV. This table is used in computing the frequency of occurrence of accounting report falsification via creative accounting practices. This used to validate the hypothesis of the study. The report of the investigation was studied and the factors responsible for the failure identified. The proportion of creative accounting-related factors to total factors was determined.

Table IV reveals that the highest rate of failure occurred in 2004 involving 24 enterprises. The rate at which enterprises fail due to creative accounting practices is increasing at a decreasing rate decreasing, compared to the rate of failures between 2000 and 2002. This decrease in number of failures is significantly due to public criticism, owners and shareholders concern and increased government regulation on auditors.

The hypothesis is tested using the statistics in Table IV. The result shows that creative accounting practices significantly influence the rate of corporate failures with an R^2 of 96 per cent. The facts are as contained in model summary, ANOVA and coefficient tables (Table V).

4.4 Consequences of creative accounting practices

The conflicts of interest among different interest groups represent the real causes of creative accounting: the managers are interested in paying less taxes and dividends, the

Year	No.	Rate of failure (%)	Cumulative (%)	CAPPC*
Prior to 1990	7	12.1	12.1	0.73
Prior to 2000	6	10.3	22.4	0.88
2000	5	8.7	31.1	0.67
2001	3	5.1	36.2	0.79
2002	24	41.4	77.6	0.89
2003	4	7.0	84.6	0.75
2004	2	3.4	88.0	0.90
2008	2	3.4	91.4	0.64
2009	1	1.7	93.1	0.81
2010	1	1.7	94.8	0.76
2011	2	3.4	98.2	0.61
2012	1	1.7	100.0	0.89
Total	58	100		

Note: *CAPPC is Creative Accounting Practices Proportional Contribution to Failure
Source: Authors' computation via Wikipedia and other Internet sources (Appendix)

Table IV. Failed enterprises, year of failure and rate of failure

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Table V.
Summary of model statistics

Model summary				
Model	R	R square	Adjusted R square	Standard error of the estimate
1	0.979[a]	0.93	0.81	10.97761

ANOVA[b]					
Model	Sum of squares	df	Mean square	F	Significance
Regression	123.763	1	123.763	1.027	0.000[c]
Residual	1,205.079	10	120.508		
Total	1,328.842	11			

Coefficients[c]					
Model	Unstandardized coefficients		Standardized coefficients	T	Significance
	B	Standard error	Beta		
(Constant)	17.280	25.464		0.679	0.001
CAPPC	32.968	32.532	0.9797	1.013	0.000

Notes: [a]Predictors: (Constant), CAPPC; [b]Dependent Variable: CF; [c]Predictors: (Constant), CAPPC; [d]Dependent Variable: CF

shareholders in gaining higher dividends, the employees to obtain better salary and higher profit share and the authorities to collect more taxes. It can be easily seen that the interests are tremendously divergent and creative accounting is deepening it because the parties are not true or fair to themselves in the pursuit of their short term objectives and in the process destroying the economy in the long term. Foreseeing the long term danger, Schiff (1993, p. 94) warned investors that taking a company's financial statements at face value can be "a recipe for disaster". The investors often go wrong by taking into consideration only one ratio, such as earnings per share (EPS); a ratio that can be "boosted by the stroke of an accountant's creative pen".

Jim Kennan, the Attorney General of Victoria, in a speech before members of the Australian Society of Accountants, pointed out that financial statements, which inflate the financial position and the performances of companies by manipulating the figures (i.e. through creative accounting) should be stamped out because it brings the investor in great difficulties to distinguish between the made up financials and the true financials. Therefore, accounting creativity is a "Pandora box". It is then pertinent to consider the consequences of creative accounting from the perspective of the practitioners. The respondents were asked to choose from a number of multiple options the consequences of creative accounting practices. Their responses are shown in Table VI.

The survey buttresses the position that these practices enhance inefficiency and leads to improper allocation of resources. It shows the faulty foundations and database for policy and investment and explains the unexplainable variable relationship in the country. It is common place to find that Nigeria is ranked BB- (Stable) not only in credit rating but also among the poorest of the poor nations. Banks are declaring huge profit and loans are non-performing and a high level of failed investments. The country ranks as one of the most corrupt countries in the world with highest level of capital flight, yet the economy is growing. Creative accounting is the root cause of policy inconsistency and is responsible for the fiscal and monetary policy failures witnessed in the country. The accumulated effects of accountants' ill-creativity fuel the cycle of economic depression. The description of creative accounting as "[. . .]. the biggest con trick since the Trojan horse [. . .]" by Griffiths (1986) is more than befitting. This creativity is a financial time bomb and the consequences are dire. The implications are better imagined than experienced.

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Consequences	No. of respondents	(%)
It creates confusion among the stock exchange investors, as the figures shown in financial statements are often inflated making it difficult for investors distinguish between the fair and unfair statements	72	90
Poor allocation of scarce resources	74	92.5
The prospectuses of the listed companies do not always offer a detailed picture the financial positions and performance	45	56
The techniques used by creative accounting can "impress the investors only over a short-term periods, while the financial position goes worse	80	100
The long term effect of such practice is the distrust of the investors conducted by the collapse of companies that take advantage of these techniques	80	100
Policy inconsistency and unexplainable variable relationship	40	50
Accumulated manipulations fuel the cycle of economic depression	68	85

Note: Field survey (2015)

Table VI. Consequences of creative accounting

4.5 Other factors that complements the negative accounting creativity

Aside from the creative practices, necessitated by the conflict of interest between owners (shareholders) and managers, there are other factors that encourage falsification and misrepresentation of companies' operations in accounting reports. These factors vary and the respondents' contributions are tabulated in Table VII.

Table VII highlights the other complementary factors that encourage this euphemism called creative accounting. This list is not exclusive. Greed by Directors and Compromised Managers and Lack of Discipline from Professional Bodies, rank the highest.

5. Conclusion and recommendations

It seems clear that in general creative accounting is seen as a deceitful and undesirable practice. In this section, we analyse some measures which can help to reduce the scope for creative accounting practices, identifying, where applicable, recent developments in International Accounting Standards (IASs). IASs will become the standard for all Nigerian listed companies from 2012. However, we state categorically that more or increased regulations will lead to more loopholes and improved manipulations. The panacea lies in the accountants and managers resolve to do what is right. What is right must be determined by the long-term economic implications of such action. It demands more of genuine creativity

Factors	No. of respondents	Relative importance (%)
Lack of auditors independence	61	76.3
Greed by directors and compromised managers	78	97.5
Legal system that encourages inconclusive prosecution	54	67.5
Lack of discipline from professional bodies	78	97.5
Lack of professional ethical foundations	59	73.8
Poor understanding of theoretical underpinnings by practitioners	45	56.3

Source: Field survey (2015)

Table VII. Factors that complements the negative creativity of accounting

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and virtue than adherence to unnecessary or non-applicable rules and regulation. Amabile *et al.* (2005) and Amabile (1996, 1998) have suggested that even this profession can benefit from the ethical application of creative thinking.

The above notwithstanding, accounting regulators who wish to curb creative accounting have to tackle each of these approaches in a different way:

- Scope for choice of accounting methods can be reduced by reducing the number of permitted accounting methods or by specifying circumstances in which each method should be used. Requiring consistency of use of methods also would help; a company choosing a method which produces the desired picture in one year will then be forced to use the same method in future circumstances where the result may be less favourable. The latest developments in International Accounting Standards are pursuing the objective of reduction in accounting choice (IASB, 2003). Adherence to these principles will guide policymakers and regulators in monitoring the excesses of the managers.
- Abuse of judgement can be curbed in two ways. One is to draft rules that minimize the use of judgement. At one time, for example, company accountants tended to use the "extraordinary item" part of the profit and loss account for items they wished to avoid including in operating profit. Again, the present rules of the International Accounting Standards have nearly abolished the category of "extraordinary item". Auditors also have a part to play in identifying dishonest estimates. The other is to prescribe "consistency" so that if a company chooses an accounting policy that suits it in one year, it must continue to apply it in subsequent years when it may not suit so well.
- Artificial transactions can be tackled by invoking the concept of "substance over form", whereby the economic substance rather than the legal form of transactions determines their accounting substance. Thus, linked transactions would be accounted for as one whole.
- The timing of genuine transactions is clearly a matter for the discretion of management. However, the scope to use this can be limited by requiring regular revaluations of items in the accounts so that gains or losses on value changes are identified in the accounts each year as they occur, rather than only appearing in total in the year that a disposal occurs. It is interesting to observe that the International Accounting Standards Board is tending to move towards valuation at fair value rather than based upon historical cost in several recent accounting standards and discussion papers.
- Rather than rely on regular audit committees to check auditors' independence, opposition led committees should be created. These committees can act as whistle blowers, criticizing every activity that deviates from what appears normal and not in the interest of the enterprise. This group stands the chance of not being compromised. However, whilst not compromised, the opposition can play a vital role in ensuring accountability, reducing negative creativity by providing the principal (owners) with adequate information for decision to enforce punishment.
- To ensure reduction in the deepening of creative accounting practices, audit procedures should be proactive. Given the current state, the agent knows when the auditors will be invited. He has enough time to rearrange himself and the events around his operations. However, the proactive approach demands that checking must and should not be annually only, it can be at any time of the year or even more

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than once. If the owners are responsible for engaging the auditors, then such audit and investigation should be without notice to the agent.

Creative accounting is the root of numerous accounting scandals. It represents the transformation of the accounting figures from what they are in accordance to the economic reality into what the managers want using the advantages of the existing regulations and/or ignoring some of them (Prerna and Anurodh, 2015). The impact of the creative or fraudulent accounting can be reduced not only by changes in accounting regulation but also by properly enforcing ethical standards and governance codes in the corporate world. Regulation without thorough enforcement techniques is likely to be ineffective in preventing individuals from employing misleading reporting practices. The challenge of enforcing International Accounting Standards within a range of differing accounting cultural contexts is likely to be problematic.

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Appendix

Company	Year	Audit firm	Country	Notes
Associated Electrical Industries, after being acquired by General Electric Company plc	1967		UK	
Pergamon Press	1969		UK	
Lockheed Corporation	1976		USA	
Nugan Hand Bank	1980		Australia	
ZZZZ Best	1986		USA	Ponzi scheme run by Barry Minkow
Barlow Clowes	1988		UK	Gilts management service. £110m missing
MiniScribe	1989		USA	
Polly Peck	1990		UK	
Bank of Credit and Commerce International	1991		UK	
Phar-Mor	1992	Coopers & Lybrand	USA	mail fraud, wire fraud, bank fraud, and transportation of funds obtained by theft or fraud
Informix Corporation	1996	Ernst & Young	USA	
Sybase	1997	Ernst & Young	USA	
Cendant	1998	Ernst & Young	USA	
Waste Management, Inc.	1999	Arthur Andersen	USA	Financial mistatements
MicroStrategy	2000	PricewaterhouseCoopers	USA	Michael Saylor
Unify Corporation	2000	Deloitte & Touche	USA	
Computer Associates	2000	KPMG	USA	Sanjay Kumar
Lernout & Hauspie	2000[1]	KPMG	Belgium	Fictitious transactions in Korea and improper accounting methodologies elsewhere
Xerox	2000	KPMG	USA	Falsifying financial results
One.Tel	2001	Ernst & Young	Australia	
Enron	2001	Arthur Andersen	USA	Jeffrey Skilling, Kenneth Lay, Andrew Fastow
Swissair	2001	PricewaterhouseCoopers	Switzerland	
Adelphia	2002	Deloitte & Touche	USA	John Rigas
AOL	2002	Ernst & Young	USA	Inflated sales
Bristol-Myers Squibb	2002	PricewaterhouseCoopers	USA	Inflated revenues
CMS Energy	2002	Arthur Andersen	USA	Round trip trades
Duke Energy	2002	Deloitte & Touche	USA	Round trip trades
Dynegy	2002	Arthur Andersen	USA	Round trip trades
El Paso Corporation	2002	Deloitte & Touche	USA	Round trip trades
Freddie Mac	2002	PricewaterhouseCoopers	USA	Understated earnings
Global Crossing	2002	Arthur Andersen	Bermuda	Network capacity swaps to inflate revenues

(*continued*)

Table AI.
List of reported accounting scandals

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Company	Year	Audit firm	Country	Notes
Halliburton	2002	Arthur Andersen	USA	Improper booking of cost overruns
Homestore.com	2002	PricewaterhouseCoopers	USA	Improper booking of sales
ImClone Systems	2002	KPMG	USA	Samuel D. Waksal
Kmart	2002	PricewaterhouseCoopers	USA	Misleading accounting practices
Merck & Co.	2002	Pricewaterhouse Coopers	USA	Recorded co-payments that were not collected
Merrill Lynch	2002	Deloitte & Touche	USA	Conflict of interest
Mirant	2002	KPMG	USA	Overstated assets and liabilities
Nicor	2002	Arthur Andersen	USA	Overstated assets, understated liabilities
Peregrine Systems	2002	KPMG	USA	Overstated sales
Qwest Communications	2002	1999, 2000, 2001 Arthur Andersen 2002 October KPMG	USA	Inflated revenues
Reliant Energy	2002	Deloitte & Touche	USA	Round trip trades
Sunbeam	2002	Arthur Andersen	USA	Overstated sales and revenues
Symbol Technologies	2002		USA	Overstated sales and revenues
Tyco International	2002	PricewaterhouseCoopers	Bermuda	Improper accounting, Dennis Kozlowski
WorldCom	2002	Arthur Andersen	USA	Overstated cash flows, Bernard Ebbers
Royal Ahold	2003	Deloitte & Touche	USA	Inflating promotional allowances
Parmalat	2003	Grant Thornton SpA	Italy	Falsified accounting documents, Calisto Tanzi
HealthSouth Corporation	2003	Ernst & Young	USA	Richard M. Scrushy
Nortel	2003	Deloitte & Touche	Canada	Distributed ill advised corporate bonuses to top 43 managers
Chiquita Brands International	2004	Ernst & Young	USA	Illegal payments
AIG	2004	PricewaterhouseCoopers	USA	Accounting of structured financial deals
Bernard L. Madoff Investment Securities LLC	2008	Friehling & Horowitz	USA	Massive Ponzi scheme[42]
Anglo Irish Bank	2008	Ernst & Young	Ireland	Anglo Irish Bank hidden loans controversy
Satyam Computer Services	2009	PricewaterhouseCoopers	India	Falsified accounts

(*continued*)

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Company	Year	Audit firm	Country	Notes
Lehman Brothers	2010	Ernst & Young	USA	Failure to disclose Repo 105 transactions to investors
Sino-Forest Corporation	2011	Ernst & Young	Canada-China	
Olympus Corporation	2011	Ernst & Young	Japan	*tobashi* using acquisitions
Autonomy Corporation	2012	Deloitte & Touche	USA	Subsidiary of HP

Table AI.

Sources: wikipedia.org/wiki/Accounting scandals, www.accounting-degree.org/scandals/

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