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# **Performance optimization – „sometimes” – result creativity**

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Seen first as an art, " dell'arte della scrittura veneziana " as he called Luke Paciolo accounting became in turn a technique , a science , a language formalized a social game and, more recently , a techno- science.

Long preserved and still used the phrase " art of manipulating figures " which is not far from the truth if we consider the professional accountant freedom to choose between two or more accounting policy choice of the best options is dependent a multitude of factors including its ingenuity .

Ingenuity , as well as imagination , novelty , originality and creativity are attributes that led the accounting field coverage of a certain reality , as desired and as there are not .

Talking about the performance is natural to ask the following questions : is there a dose of fiction in it ? , That the steps in obtaining and menținerea performance management may be considered constructive practices and practices with negative meanings ?

**Keywords:** Accounting, creativity, performance, gain, competitive advantage

**JEL classification:** M200, M410

## 1. Introduction

The quality of a fable, says I.C.Lungu (2006)<sup>1</sup>, is to represent an image of reality, but the convenience of the creative spirit is more easily pass the imaginary imagination, from researching a truth hidden under the appearance admission truths of seemingly adapted dorinețelor each. That motivates ICLungu accounting innovation that contributed to the emergence and development of creative accounting sitting at the boundary between legal form and economic substance of transactions and events.

Bias in coverage of "economic reality" of the company is based on the flexibility in the application of accounting principles, the application of professional judgment. This flexibility has led to cases of creative accounting.

Creative accounting concept first appears in literature in 1973, in the British researcher's work J.Argenti. According to him, the creative accounting practices, with incompetent management, leading to intensification of business decline, the harbinger of economic crisis.

If assimilate views on the definition of creative accounting, note that this axis "extends from a genuine attempt to present a fair picture to the practice of "off-balance sheet financing 'and' Finishing 'balance sheet".

In contrast, the authors are rather creative accounting as a means to optimize a company's financial position and performance, created especially benefit accounting normalization adopted internationally.

## 2. Motivational context of the development of creative accounting practices and their role in optimizing performance

The diversity of views on the definition of creative accounting and the various forms that takes, and "existential complexity" that manifests makes it become fertile ground of strategic and tactical approaches, initiated and carried out in recital one objective, that of creating a distorted image on firm performance.

Performance of firms in the primary sense is assessed by positive financial results that the company obtained. Deformations performance can only be done by a manager, leader ('force') in control. Over time, researchers have extensively discussed "power rush", identifying two actors in power: those who possess (shareholders) and those in control (managers).

Managers' ability to control resides in possession of information "in pure form" (eng. information perspective), information that gives them power to decide who may or may not in line with the expectations of shareholders of the company.

At the firm level, hierarchical features of "ends" involved in leadership (managers and company shareholders), dictate 'quality' transfer of information and direction ("granted" self-interest). To achieve "s targets", managers can "filter" in an opportunistic public information.

Various situations in which shareholders are under instrumentarul chemical relationship between characteristics and awareness generator capable of influencing decisions (positively or negatively depending on the perspective of analysts) determines a conflict of interest in relation to managers or employees, in which awareness fuels generally unsubstantiated decisions on analyzing the factors that generate revenue but to analyze factors generating costs.

This conflict of interest developed around the standard "gain" on which work is appreciated managers under contracts between the parties. If the contractual terms, value, subordinate in most of criterion "win" when measuring performance (firm value) only this criterion, dilute the importance of accounting information, thus losing their intrinsic value.

Focusing our attention on the approach based on contract costs, identify network interconnections subordinate managerial interest:

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<sup>1</sup> Lungu, I.C. – „Politici și tratamente contabile privind evaluarea performanței financiare a întreprinderii”, Teză de doctorat, ASE București, 2006, pag.274

- the remuneration of managers depends on the income distributed to owners (noting the managerial);
- the first employees depend on the "goodwill of the owners."

As shown in the second approach, the information taken new dimensions and the strategic properties it holds, gives managers "opportunity" to take decisions that affect the financial results. The discrepancy between the amount and quality of information held by a company's strategic tip gives rise to the concept of asymmetric information.

"Status" information asymmetry lies in the fact that some (management) has an informational advantage compared to other (Shareholders).

WRScott (2009)<sup>2</sup> identified two types of asymmetric information:

- adverse selection "is a type of asymmetric information in which one or more parties in a financial transaction or a potential transaction has / have informational advantage over other parties";
- moral hazard "is a type of asymmetric information in which one or more parties in a financial transaction or a potential transaction can observe their actions in carrying out operations in return the other party can not."

On line accordingly, shareholders versus managers can manager earnings and how they do not give birth or management technique results "earnings management", from which we identify the motivational context of the development of creative accounting practices. For this, we display "fan" the definition of "earnings management" on the diagram interrogative:

how?	what?	why?
...	...	...

According to the authors C.Mulford and E Comiskey (1996)<sup>3</sup>, "Activities of earnings management is handling accounting results in order to create the impression of firm performance."

how?	what?	why?
<b>the art of manipulation</b>	<b>accounting results</b>	<b>Image of enterprise performance</b>

In 1997, W.Scott<sup>4</sup>, believes that "given that managers can choose from a set of accounting policies is normal (natural) to expect that they will choose policies such that, to maximize their own utility (wealth) and / or the market value of the company. "In 2008, repeating the theme of financial accounting theory states that earnings management is limited to election managers, accounting policy choices designed to achieve the specific goals.

how?	what?	why?
<b>Flexible legislative</b>	<b>Toolbox - accounting Policies</b>	<b>specific Objectives</b>

Amid spur development of earnings management ethics degradation SEC took action to expose abusive earnings management practice that the supposed "hoax, using various forms of brilliant ideas - to distort the true level of performance of a company, in order to obtain desired results "<sup>5</sup>.

how?	what?	why?
<b>abusive actions</b>	<b>The level of corporate performance</b>	<b>Desired results</b>

<sup>2</sup> W., R., Scott - *Financial Accounting Theory*, 5tr edition, Prestige Hall, Toronto, 2009, pag.13-14

<sup>3</sup> C., Mulford, E., Comiskey, *Financial Warnings*, New York: John Wiley & Sons, 1996, pag. 360

<sup>4</sup> Scott ,W., R., - *Financial Accounting Theory*, Englewood Cliffs, NJ: Prentice-Hall, 1997, pag. 295

<sup>5</sup>Securities and Exchange Commision, *Annual Report*, Washington, DC, 1999, pag. 84

Likening it with a loose management author K.Schipper<sup>6</sup>, defines as "deliberate intervention in the external financial reporting in order to get some private gain, unlike / totally different than just facilitating the neutral operation of the process".

how?	what?	why?
Power to intervene	The financial raporater	Getting personal gains

P.Healy and J.Wahlen authors consider that managers' use judgment in financial reporting and in structuring transactions to amend the financial statements in order to mislead or some stakeholders about the underlying economic performance of the company or to influence contractual outcomes that depend on reported accounting numbers "earnings management

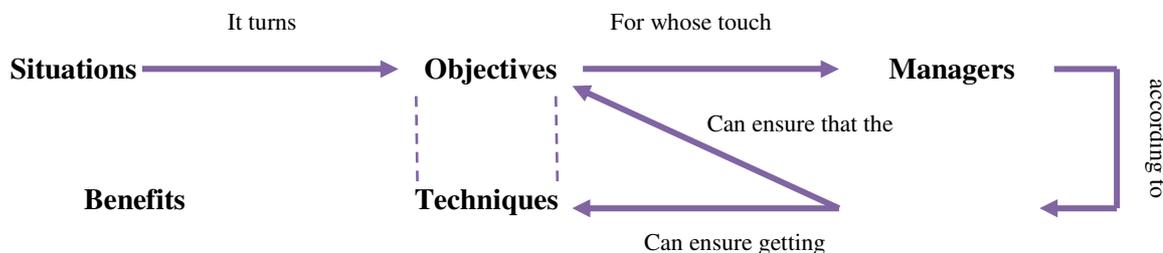
how?	what?	why?
The power to decide	financial reports	Create an altered image on the economic performance or to influence the results of the underlying performance of contracts

Having identified WHO IS (ARE POWER) to pimp up and create a desired image of the company, depending on personal needs (professional), we present theoretical and practical consistency of each proposed interrogative questions, namely: Why? - What? - How?

In explaining WHY? -'s, We leave the "game awards" ( Rewards of the game), proposed by teachers and EEComiskey CWMulford<sup>7</sup>.

Reaffirming the central question of the paper „The Financial Numbers Game: Detecting Creative Accounting Practices”: *Do the numbers (financial results) make sense?*<sup>8</sup>, Propose the plan of "unmasking" creative accounting practices, a journey through the most representative elements identified by the authors, we try to bring economic record books.

We believe the answer to the question: **what creative accounting practice?** because ... **Every situation requires action, and action requires a result, an interest, an advantage. In this context we propose the following scheme of conditioning elements:**



Source: Belongs author

Figure 1. Decision-making process

The complexity of inter-network in which a firm operates and diversity assembly requirements that must respond in order to maintain a competitive face various situations whose solutions ensure feedback.

Thus, ensuring an adequate response to the situation created conjuncture resolved by appropriate techniques "target's" reached creates prerequisites to obtain the following

<sup>6</sup> Schipper, K. 1989. Commentary on Earnings Management. *Accounting Horizons* (Vol. 3, No. 4), pag. 92

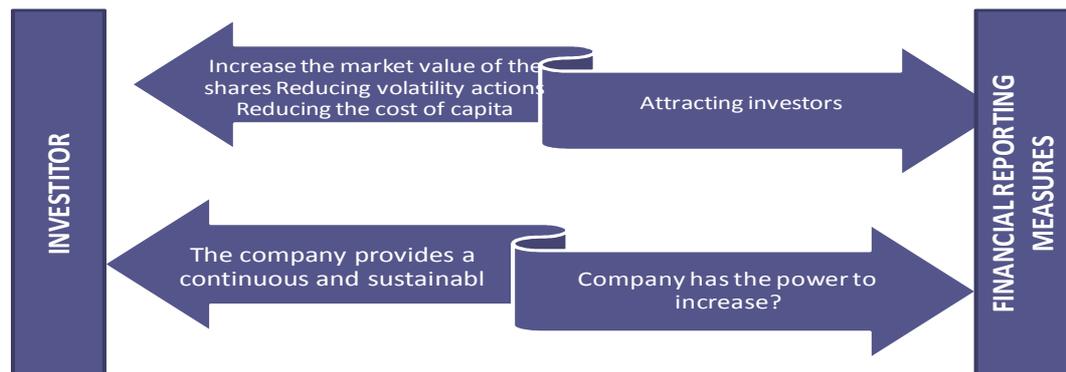
<sup>7</sup>In 2002, professors Charles W. Mulford and Eugene E., Comiskey have published the paper "The Financial Numbers Game: Detecting Creative Accounting Practices." Within this creative accounting issues discussed, theoretical and practical aspect. The stated goal was to help users of financial statements to identify creative accounting practices.

<sup>8</sup>Lait motiv pentru lucrarea „The Financial Numbers Game: Detecting Creative Accounting Practices”

advantages:

**✚ Increase the company's market value (share price effect)**

One of the techniques by which management can ensure continuity and sustainability of the firm's revenues image is the one called " rainy day raising money ," which , even in the less profitable by making adjustments in value in years very good financial results , as revenue can ensure the stability of positive financial results . I mention that in value adjustments for uncollected receivables or provisions for guarantees to customers , in years with good results, even if at the time of establishment diminish their profits , representing as expenses at the time of collection they transform into revenue recoverable that the cash flow attracted allow development of the company and hence the company's stock market value . The advantage of increasing the company's market value by practicing creative accounting is shown in Figure No. 2



Source: Belongs author

Figure 2. *The advantage of increasing the market value of the company through creative accounting practices*

Thus, in less good , you just picture looks good because creative accounting firm , management can create opportunities for future revenue generation . An alternative would be to invest a portion of profits to create a technical facilities / equipment performance , which provides a solid foundation for developing business activity in the medium or long term , even if short-term is a reduction in income to shareholders.

At the same time , addressing some of the profits are reinvested in assets to diversify activities related to effective management is a technique combining diversification with durability .

Shareholders with a keen sense of reality will appreciate and accept this approach effective management perspective that is generating sustainable profits .

Investors (potential ) are interested primarily of capacity / growth of the company . Through creative accounting techniques can improve financial reporting measures so that the company's financial statements show that it can provide a continuous and sustainable revenue and in conjunction with an appropriate policy active , this can materialize in cash flow flow ( oxygen , the catalyist of any activity ) .

Under the influence of such images , " aphrodisiac " , investors are willing to pay to " play " the same " game" as participants - shareholders whose wealth increases. By attracting investors , the company will have a " feed -back strength" - increasing the market value of the shares, reducing the volatility of shares, reducing the cost of capital - immediately resounding impact in terms of image, the other potential investors willing to pay higher prices.

**✚ Improved lending conditions (loan cost effect)**

The same principle is checked and contractual relations with credit institutions. In general, firm performance assessment criteria cover both the quantitative (outcome indicators) as well as qualitative (stability, continuity, development). Thus, though creative accounting practices ensure income stability without their correspondence availability, the company does

not provide security, something that can be compensated only by the effective management of creative opportunities.



Source: Belongs author

Figure 3. *The advantage îmbunătățirii credit conditions through creative accounting practices*

Credit institutions assess credit rating of the company, regardless of financial contact - contract or renegotiation. Through creative accounting techniques, proper influences evaluation indicators, the company can obtain favorable credit terms - relaxing financing contracts under "move upward",<sup>9</sup> reducing costs of existing loans.

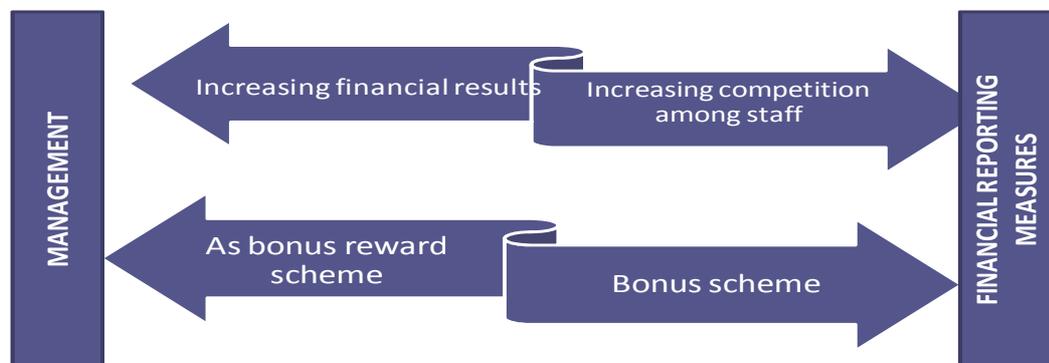
Increasing safety credit quality allows the company to be "courted" for suitable offers new "level bargaining" obtained.

✚ **Increasing financial results (the effect of the bonus)**

Creative accounting exposed unaccountable manipulation techniques results amid the momentum employees bonus plans .

The desire to increase accountability and individual involvement in the act of management, some companies build schemes reward - motivation bonus in the form of X % of profit or opportunity to purchase shares " employee of the year " which grossed over £ Y , Z consecutive months , etc. .

In this regard, employees may use various creative techniques for obtaining and reporting the desired result , which will generate growth fictional artifice of various indicators . Effective management will use various successful practices to determine not only the employees to perform their work but even to achieve excellence . Thus , a good manager will know to capitalize the main attributes of effectiveness in coordinating employees , using a proper relationship in which authority is recognized and accepted by employees and which are driven accountability for performance tasks.



Source: Belongs author

Figure 4. *Growth advantage results through creative accounting practices*

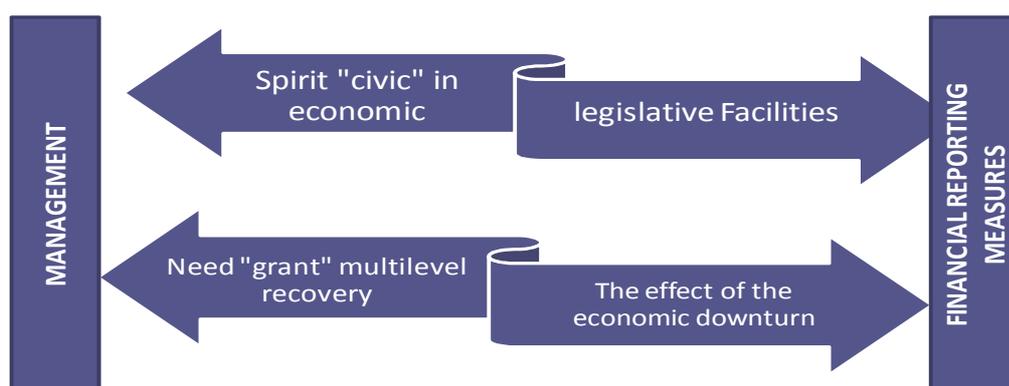
<sup>9</sup> Ramp recovery due to reduced cash cost of the "dedicated"

Meanwhile efficient management will know how to mobilize employees in the desired direction, using effective communication techniques and the application of transactional analysis in their management. Finally, using the elements of organizational culture to train employees to influence their behavior, by reshaping the organizational culture and effective application of airway management.

Manager plays an important role in controlling the activity consistently supported employees, whose dedication to sustainable growth of the company. Therefore, we conclude that the work of human capital, although difficult to quantify the activity itself, will certainly generate consistent financial results for the company.

#### 🚩 Reducing taxes (effect "Portiței" legislation)

For recovery in situations of recession, the state can provide a range of relaxing and supportive measures economic, fiscal, which will harness effective management prompt.



Source: Belongs author

Figure 5. Advantage of tax relief through creative accounting practices

For recovery in times of recession, the state can provide a range of relaxing and supportive measures economic, fiscal. Through creative accounting techniques can shape financial reporting measures, such as to "meet" criteria "unfavorable" required by the legislation.

In this respect, we mention some techniques that can "demitifica" financial results, such as:

- technique "rainy day raises money" that I mentioned earlier will be used to reduce profit by increasing spending, creating reserves in the form of bad debt provisions, guarantees to customers in the years in which financial results are not supported receipts to the invoices;
- control technique that revenue by increasing spending, using forms of accelerated depreciation of assets or opting for lower residual values at the acquisition of fixed assets;
- technique "big bath" that the poor financial results, considered sacrificial, opting for those measures to increase spending, respectively worsen more, financial situation, leading to firm employment accessibility grid facilities tax.

Effective management will use the tax benefit created in the development of activities that will counterbalance the assembly generated taxable items (assets, human capital and financial).

As presented, the gross manifestation **forms of creative accounting techniques only generate image benefits, intangible. Their inclusion in effective management practices will result in a set of levers which can act on material factors, human, financial impact in creating perceived benefits** in terms of continuity and ensuring cash flow without a firm not and can exploit the potential of the image.

## 2. A new practical performance optimization - imputing costs for raising capital on the first issue

We ask ourselves: accounting victim or guilty? and which can not only answer the following:

- ✚ accounting is a victim? We believe that the accounting information provided are those required by the market. To that end accounting is a victim of its past success;
- ✚ accounting is guilty? Yes, because when we try to predict the future introduce a large variability in the results, and if we think we can do this with a certain level of reliability, we are equally guilty of inducing error that users will not believe the information provided by companies

**The solution?** is only one, namely the presentation of financial statements that contain simple data more reliable and easier to understand. If accounting provide relevant information, then why not reply to the message? Accounting can be a credible messenger? Absolutely yes, in so far as it respects the accounting rules or provide all relevant information on the most complex transactions of the company, by way of notes.

I did notice that this plea for continued international concerns creative accounting professionals in finding new ways to optimize the results. These lists, and increase capital expenditure imputation on issue premiums.

In France, for example, is regulated able to pass increased capital expenditures related to the first issue of this growth. To show this approach we refer the example presented H.Stolowy a fictional example as stated by the author, relative to firm Berry who proceeded to the capital increase in cash by an investor with the amount of 5.500.00 F, of which 4,500 .000 F premium. The capital increase was based on the financial situation on 30 September and attracted a number of charges, as shown in Table 1.

Expenditure	Amount
Intervention Society lawyer who negotiated and drafted shareholders agreement	40.000
Intervention Advocate investor	50.000
Payment of legal counsel, the university professor, the disagreement	20.000
Legal audit conducted by attorney investor	30.000
Intervention chartered accountant to check the company's interim report sheet	15.000
Accounting audit performed by a cabinet mandated by investor	100.000
The auditor's report on the suppression of subscription rights	10.000
Performing legal related expenses (legal notice, stamp duty ...)	10.000
Intervention marketing consultant business plan	130.000
TOTAL	405.000

Table nr.1. *Situation of increasing capital expenditure*

Berry company managers decide to include all costs incurred in growth capital expenditures (if our regulations mention up costs). In addition, add the time spent growing operation and capital expenditure forms part of the capital increase in the form of wages and social spending which amounts to 145,000 F. Therefore the total costs of the capital increase will be 550,000 F and 10% of capital growth.

In support of the idea of crossing the increase of capital expenditure on the first issue is motivated by the author as follows:

- accounting texts are less precise regarding the exact nature of growth capital expenditures;
- attribution of costs on the first issue "does not hurt anyone" because it has the effect of increasing earnings in the year in which the capital increase and equity does not change. Where, says the author, can be considered two ideas:
  - tax is not affected because the accounting and tax increases. If at first be entered in the assets, they are excluded from the deductible expenses. Secondly, the attribution of the first issue is the suppression effect subsequent depreciation;
  - enterprise value does not change as equity are at the same level and, therefore, shareholders have no reason to complain
- even if equity are the same, whatever the amount of the capital increase, the result is changed. However, users of accounting information usually is interested on the development results and less on the evolution issue premiums.

In the practice of our country, expenses arising from the capital increase shall be governed by OMPF 3055/2009 as formation expenses (expenses on issuance and sale of shares and bonds, and other expenses of this nature, the extension of the entity). Such expenses may be included in the "active" if it immobilizes (basically there are 201 account "expenses") and amortized within a period not exceeding five years.

Apparently, as our regulations, at the time of the capital increase, the results are not affected, but their payment obligation clearly contributes to the gradual reduction of the results. This leads us to support the French practice and agree with the costs related to the capital increase of the amount of issue premiums that it generates.

Accounting solution covers two possibilities:

- be through Account 721 "Income from production of intangible assets" if they are initially recorded at cost, and account 201 "expenses" for the capital expenditure growth have Amending the role of the first issue;
- be keeping the current methodology, but not to recover and in time of removal of the first records to be passed on the issue.

**The conclusion** we reach based on those presented in this paragraph and the previous ones is that in order not to attract attention to the negative impact of investment business leaders resort to earnings management and use various levers (mechanisms, tools, processes) growth accounting results. Increase results should reassure investors and lead to a better assessment of the business.

In fact, companies that have a large free cash flow are more geared towards finding the "accruals" <sup>10</sup> discretionary increase results, in the opinion of R.Chung et al. (2005) <sup>11</sup>.

#### 4. Conclusions

Specialists economists who launched the concept of "creative accounting", the relational term with a negative connotation, but in our view this connotation can be changed in circumstances where there is an effective management that using certain attributes of creative

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<sup>10</sup> accruals = all income and expenses recorded in the income statement and not give rise to any flow during the year. We consider the nature of depreciation expenses and revenues , creation and reversal of value adjustments , creation and reversal of provisions ... ) and expenses and deferred income ( constituents variation of working capital requirements ) . Watts and Zimmerman ( Watts RL, Zimmerman JI (1990 ) , " Positive accounting theory : A ten year perspective " , The Accounting Review, vol 65, n ° 1 , pp. 131-156 . ) Had the advantage of measuring global incidence alegereilor all accounting and aggregate all the effects of changes in accounting policies kept alone. Some of these adjustments , called non - discretionary comes from the normal activity of the company and shall be deemed not suffer any managerial discretion . Another part , discretionary company is managed by leaders intentionally used to detect management results.

<sup>11</sup> Chung R., Firth M., Kim J.B., - « *Earnings management, surplus free cash flow, and external monitoring* », Journal of Business Research, vol. 58, n° 6, pp. 766-776., 2005

accounting can capitalize the entire activity of the company, including the creation of the necessary liquidity.

Thus, replacing the word "handle" used by authors C. Mulford and E. Comiskey verb "present", we propose the following definition of management results corresponding timeliness of economic life: results management is a whole generation techniques and presentation of accounting results order to promote enterprise image performance.

What makes the difference is the development of strategies, depending on the impact of the results, subject to the time dimension. Financial results generated only through creative practices of classical (under immediate benefit) does not create the prerequisites for sustainable development.

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