Concept of Creative Accounting and Its Different Tools

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ABSTRACT:

Our study shows the Concept of Creative Accounting and its different tools used for doing Creative Accounting. We reviewed different articles taken from Jstor, Emerald, and Science direct and Repec.org etc. and explained different methods of creative accounting and who gets benefit from this. We also explain solution part of Creative Accounting, How it can be minimized or how we can reduce the effect of creative accounting on the Balance sheet of the companies. We discussed also how it has landed some companies into crises like Enron and world.com etc. and also save companies to land into crisis.

Key words:
Creative Accounting, Corporate Governance, Creative Disclosure Framework, Financial Scandals, Financial Reporting, Sarbanes-Oxley


1. INTRODUCTION

When we open this true Pandora’s Box: Creative Accounting then we understands when and why exactly the concept first appeared and what influenced its development that arose many questions.

With hindsight a few favorable circumstances to this concept can be identified, circumstances first related to the economical advent of world states but at the same time to need of economic entities to create for them a good reputation in an increasingly competitive and tough economic environment. About this particular moment, that is first mention belongs to the founder of accounting Luca Paciolo. This ambition of making figure more appealing or opposite is as old as 500 years. Thus, Luca Paciolo was shaping in his already renowned De Arithmetica, the first accounting manual, practices of creative accounting.

Creative accounting refers to accounting practices that may or may not follow the letter of the rules of accounting standard practices but certainly deviate from those rules and regulations. It may be characterized by excessive complication and using innovative ways of characterizing income, assets and liabilities. Some times word like “innovative” or “aggressive” are also used for defining creative accounting. Creative accounting is a term which is used as a systematic misrepresentation of the true and fair income, liabilities and assets of corporations or organizations.

1.1 Definitions of Creative Accounting

Creative Accounting refers to the use of accounting knowledge to influence the reported figures, while remaining within the jurisdiction of accounting rules and laws, so that instead of showing the actual performance or position of the company, they reflect what the management wants to tell the stakeholders.

“Purposeful intervention in the external financial reporting process with the intent of obtaining some exclusive gain”.

“Creative accounting is the transformation of financial accounting figures from what they actually are to what preparer desires by taking advantage of the existing rules and/or ignoring some or all of them”. (Kamal Naser, 1993:2)

“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. It is creative accounting.” (Ian Griffiths, 1986:1)

‘Is the deliberate dampening of fluctuations about “some level of earnings considered being normal for the firm”’. (Barnea et al. 1976)

‘Is 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)
‘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)

Schipper (1989) observes that ‘creative accounting’ can be equated with ‘disclosure management’, ‘in the sense of a purposeful intervention in the financial reporting Process’. Many terms can be used to describe the practices of changing the facts in accounting, e.g. cooking the books, aggressive accounting, massaging the numbers, window dressing, earnings management, etc.

**TABLE No. 1- Common Labels for Financial Numbers Game**

<table>
<thead>
<tr>
<th>Label</th>
<th>Definition</th>
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<tbody>
<tr>
<td>Aggressive Accounting</td>
<td>A forceful and intentional choice and application of accounting principles done in an effort to achieve desired results, typically higher current earnings, whether the practices followed are in accordance with GAAP or not</td>
</tr>
<tr>
<td>Earnings management</td>
<td>The active manipulation of earnings toward a predetermined target, which may be set by management, a forecast made by analysts, or an amount that is consistent with a smoother, more sustainable earnings stream</td>
</tr>
<tr>
<td>Income Smoothing</td>
<td>A form of earnings management designed to remove peaks and valleys from a normal earnings series, including steps to reduce and “store” profits during good years for use during slower years</td>
</tr>
<tr>
<td>Fraudulent financial reporting</td>
<td>Intentional misstatements or omissions of amounts or disclosures in financial statements, done to deceive financial statement users, that are determined to be fraudulent by an administrative, civil, or criminal proceeding</td>
</tr>
<tr>
<td>Creative accounting practices</td>
<td>Any and all steps used to play the financial numbers game, including the aggressive choice and application of accounting principles, fraudulent financial reporting, and any steps taken toward earnings management or income smoothing</td>
</tr>
</tbody>
</table>

**FOLLOWING ARE THE TECHNICAL FACTORS IN THE USE OF CREATIVE ACCOUNTING TECHNIQUES**

Intensity of competition in a context of crisis; degradation results and financial position; need financing; insufficient equity, the need to meet certain indicators especially coming from investors and analysts; desire to ensure a stable course to launch private companies wish to be given listed. The above following factors deserve to be quoted, without an order of priority Accounting for pension reserves, capitalization of costs, investment accounts and short-term claims of customers, accounting for inventories of tangible and intangible assets and accounting for long-term debt is not an option and some creativity. Therefore we can say, maybe in a provocative manner that in these circumstances, there is possibility of creative accounting.

**FOLLOWING ARE THE TECHNIQUES USED FOR CREATIVE ACCOUNTING**

1. **TANGIBLE ASSETS**

(a) The practice of "subjective depreciation" of assets creates proper field of creativity in accounting, if the management company seeks an attitude "optimistic" about the outcome, will appreciate that there are no indications that the asset has suffered depreciation, thus avoiding diminishing results. On the opposite side, In the exercise of professional reasoning, IAS 36 requires that at each balance sheet date to determine whether there are indications that the asset depreciation suffered analyzed. If management estimates that the recoverable value is lower than the net accounting assets are considered impaired for the difference. In this case the result will be affected by recording a depreciation expenses.

(b) The lease-back as the impact of a value that will be established in the year of sale, results. Charges will be recorded during the same year of leasing contract.

2. **GOODWILL**

Underestimated or under valued assets purchased leads to increase goodwill. Capitalization and depreciation of goodwill that during its useful life have influence on the outcome of further coming years. Cost of goodwill amortization resulting from the reduction outcome, with the exchange rate and competitiveness of the shares bids competitive. Charging goodwill to equity to reduce their lead, the result of years of future costs are not influenced by goodwill amortization.

3. **DEPRECIATION**

Option for a particular method of depreciation or otherwise in connection with the accounting policy of the
undertaking, the assignment in a systematic way the depreciation of an asset during its useful economic life has an impact on the profit and loss. Thus, a different method of depreciation has a different impact on the Balance Sheet. Depending on the method chosen is amended in time allocation of expenditure. Options on different useful life leads to different expenditure.

E.g. Switching from Straight line Method to Diminishing Balance method will lead different results in outcomes. As per Income Tax Law Diminishing Balance Method is more suitable for income tax calculation. Straight line method will provide less depreciation as compared to Diminishing Balance Method in late years of a life of the assets and will show more profits.

4. INVENTORIES

The inventories provide sufficient opportunities for creative accounting and subjectivism. An error detected on a voluntary basis in determining the size of existing stock in assets at the end of exercise can lead to a practice of “polishing” of the result, meaning that the underestimation or supraevaluareau stock finally has an impact not only on the financial statements of the current year but also on the following year. Inclusion in stock inventory or death is a moral waste handling method. If stocks or death moral waste will be removed from management, spending will be affected, with consequences on the outcome in the sense acestuia La reduce the opposite side, the management company can show a atitutudine optimistic, considering that these stocks will be dead recovered, especially in the situation of an economic recession. The inclusion of financial costs in the cost of production of stocks has the effect of the increase in the outcome in which the inclusion of expenses. On the opposite side, where the management has a pessimistic vision of the outcome, the result will apply the method, treating interest expense as an element of the power exercised.

5. PROVISIONS FOR LIABILITIES AND CHARGES

Practice provision (increase and reduction thereof) is an effective tool for “leveling” outcome of the company. Establishment of provisions in those years where the profit result leads to the decrease, while the resumption of the provisions in the income year in which the registers deficit increase leads to the result.

6. CONSTRUCTION CONTRACTS

Choosing between the two methods of construction contracts accounting has the following impact on the profit and loss under the completed contract, the result will be recognized at the completion of the contract. Based on the percentage of the definitive result will be spread over time, throughout the progress of the contract. Switching from one method to another has also a significant impact on the profit and loss.

2. OBJECTIVES

Objective of the study is to find out the Different types of creative accounting mean how many ways creative accounting may be done and what are the solutions of creative accounting so that the effect of creative accounting may be minimized. Relationship between corporate governance and creative accounting. Ethical behavior of auditors to reduced the effects of creative accounting.

Who are the parties who will get the benefits of creative accounting and what is the after effect of creative accounting on the life of the organization. We also try to look on the accounting standard parts which allow creative accounting and how it should be modified by the accounting authorities to reduce the effect of creative accounting because in present scenario, the accounting standards have some loopholes which provide alternative methods of accounting e.g. Recognition of revenue, methods charging for depreciation, recognition of cost etc. We also look to different tools of creative accounting, which help to reduce or increase profit as per favorable situation.

3. REVIEW OF LITERATURE

Hussey & Ong (1996) stated that creative accounting first became very prevalent in the 1980. Due to loopholes of accounting regulations, companies could produce accounts which flattered their financial performance. It talks about type of creative accounting like capitalizing interest, brand accounting, methods of depreciation, stock valuation, and accounting standards which prevent the major abuses which used to occur and has issued a number of regulations in the form of Financial Reporting Standards. The main approaches which help accounting reader and prevent creative approaches by companies are:

FRS 1 Cash Flow Statements
Profit was easy to manipulate according to critics of creative accounting and therefore Accounting Standard Board therefore issued FRS 1 which requires most of the companies to publish cash flow statement. Although there are some technical problem with it.

FRS 2 Accounting for Subsidiary Undertakings
In the 1980’s, there were a number of complex schemes where companies could bring profit without disclose their source of income and hide certain liabilities and assets from its balance sheet by operation of subsidiary style operations.
FRS 2 makes more transparent relationship between a holding company and its subsidiaries.

**FRS 3 Reporting Financial Performance**
This was a significant standard and has transformed the appearance of the profit and loss account, and also introduced some new financial statements. Instead of concentrating on single figure profit Accounting Standard Board considers companies to disclose information which reflects the various elements which make profit up.

**FRS 4 Capital Instruments**
This standard has the objective of ensuring that capital instruments are shown in financial statements in such a way that truly reflects the obligation of the issuer. Under this standard there was a clear definitions as to what must be shown as a debt, non-equity shares, and equity shares with clear rules.

**FRS 5 Reporting the Substance of Transactions**
In the past it has been possible for companies to report transactions in a way which has been legally correct, but has obscured the reality of the economic transaction. The standard attempts to rectify this by setting out definitions and the appropriate accounting treatments, particularly for transactions like consignment stocks, sale and repurchase agreements, and factoring of debts.

**Naser (1992)** stated that much is written about Creative accounting and about the various schemes of window dressing and off-balance sheet financing and very little information is available how widely such schemes are used by various companies. He has done a little empirical study to find the relationship whether creative accounting is related to the types of companies or industrial classifications, the reason behind the use of creative accounting, perceived legitimacy, consequences of the continued use of creative accounting, and measures to be taken to minimize its use. Because of much concern topic about creative accounting, it was difficult to obtain data from companies about their own creative accounting practices. However, it was felt by researchers that external auditors ought to represent an alternative source of creative accounting providing that their client information will keep secret.

In 1988, they sent copies of questionnaire to auditors and companies and got 15(out of 22) respondents that had had experience of auditing companies (7%) never encountered problem of creative accounting, 73% had found between 1 and 5 examples and 3(20%) had come across more than 5 examples. In this research he finds from his sample that private companies provided most frequent encountered examples of creative accounting and interesting was that all companies appears to make some use of it. Similarly for industrial classification, the result was that creative accounting was likely.

**Smith (1998)** classified accounting firms as “structured”, “intermediate” or unstructured in terms of their audit methodologies. Using US data at a time when the Big 8 auditing firms still predominated, he classified 22 auditing firms. The number of accounting income increasing policy changes was higher for “structured” auditors and massively lower for “unstructured” auditors. Smith also reported on the accounting manipulations employed by 208 of the largest quoted UK companies and identified 12 different techniques in the common use, all of which would impact on the Profit and Loss account and Balance Sheet of the companies concerned.

The techniques specified can be described as follows:
1. Extra ordinary and exceptional items,
2. Pre-acquisition write down,
3. Deferred consideration on acquisition,
4. Disposals- profits on sales of asset taken “above the line” and deconsolidation of subsidiaries in anticipation of sale.
5. Brand Accounting- capitalization of assets,
6. Off-balance sheet finance,
7. Contingent liabilities,
8. Changes in depreciation policy(Method),
9. Capitalization of costs (interest and R&D ),
10. Currency mismatching between borrowing and deposits,
11. Pension fund surplus used to reduce annual charge,
12. Convertible with premium put options or variable rate preferred stocks.

Out of above 12 techniques, those seven numbered as: 1, 2, 4, 8, 9, 10, and 11 having a cleared income effect. Accounting policy change with an income effect is less clearly attributable to an auditor effect in U.K. study than his earlier Australian study.

**Cosmin (2010)** described the various techniques used by the managers to get desired results. A census (not exhaustive) of the techniques used in creative accounting:
1. **Tangible assets**: “subjective depreciation” of assets creates proper field of creative accounting of management estimates that recoverable value is lower than net accounting assets are considered impaired for difference. The result will be affected by recording a depreciation expenses.
2. **Goodwill**: Goodwill increases by underestimation of assets purchases capitalization and depreciation of goodwill during its useful life have influence on the outcome of further coming year.
3. **Depreciation**: Option for depreciation method has impact on the profit and loss during useful economic life of an asset. Thus, a different method of depreciation has different impact on outcome. An option on different useful life leads to different expenditure.
4. **Inventories**: The inventory provides sufficient opportunities of creative accounting and subjectivism. The under estimation or over estimation of stock finally has an impact not only on the financial statement of current year but also on the following year.

5. **Provisions for liabilities and charges**: A practice provision (increase and decrease thereof) is an effective tool for “leveling outcome”. Establishment of provisions in those years where the profit results lead to decrease, while the resumption of the provisions in the income year in which the registers deficit increase leads to the result.

6. **Construction contracts**: Choosing between the two methods of accounting for construction contracts has the following impact on the profit and loss: - Under the completed contracts, the result will be recognized after the completion of contract, while in method based on percentage of definitive result will be staggered over time, throughout the progress of the contract switching from one method to another method also impact on profit and loss account.

Mechanisms that have an impact on the balance sheet will be listed in the following table:

**Elisabeta & Beatrice (2010)** talking about agency theory in the field of creative accounting, which relates to the conflicts of interests between users of accountancy information.

An agency relationship comes into existence when one party, known as the principal, entrusting management of their assets to another party, known as agent, who has competence and knowledge inaccessible to the principal. The most common form of agency is that in which a manager operates on behalf or a shareholder.

From this point of view in the life of an enterprise. We can identify two categories of actors having a special position (Feleaga N., 2006).

- On one side, the shareholders, who have rights after the creditors, suppliers, employees etc. they take the financial risk justifying the appropriation on a part of the year’s profit and from the case of the entity closing down,
- On the other side, the leaders because they have privileged information, taking into account the position held in the enterprise and, therefore are tempted to take advantage by allowing themselves considerable advantages or generally by, directing the entity towards a direction which is useful for them.

The conflict of interest among different interest group is the real cause of creative accounting. Managing shareholders interest is to pay less tax and dividends. Investor-shareholder wants to get more dividend and capital gains. Country’s tax authorities like to collect more and more taxes. Employees want to get better salary and higher share in profit. But creative accounting puts one group or two groups to advantageous position at the expense of others.

The IASCs framework for preparation and financial statement, envisaged by the IASB. Presents the following categories of users: current on potential investors, employees, creditors, suppliers and other commercial creditors, client, government and governmental institutions and the general public. They may be divided into internal and external users.

Internal users are principally management personnel within the company. They have responsibility to release information and external users come into other categories.

The investors can be divided into four sub-groups: real and potential shareholders and the real and potential stakeholders.

Managers may or may not believe in market efficiency. In case they do not, they can under to manipulate the number to reduce the cost of capital and to satisfy demand of external existing shareholders, to increase their own remuneration, to decrease the overall risk of firm, or to avoid violating the debt covenant or incurring political capital costs.

<table>
<thead>
<tr>
<th>Table no. 2- Potential gains and losses in/from manipulating accounts</th>
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<tr>
<td>Players</td>
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<tr>
<td>Managers</td>
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<td>Existing shareholders</td>
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<td>Existing bondholders</td>
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<td>Employees</td>
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</table>
Increase the remuneration from an unexpected Bankruptcy

Suppliers
Keeping their client Some money following an unexpected bankruptcy

Clients
Continuous services Warranty respected Services interrupted Warranties not honored

State
Tax to collect Jobs for people No more tax to collect Unemployed people to provide for

Bankers
Repayment of the loan Some money following an unexpected bankruptcy

Society
Keeping the job Production of wealth Jobs lost and resources wasted


Shah, Butt, & Tariq, (2011) tried to give answer that why do managers do creative accounting and how they become successful in performing such practices in the presence of stringent rules and procedures. They also tried to explore whether creative accounting practice is good or bring crisis in the companies and link of corporate governance with creative accounting. Many world examples given like Enron which show higher profit than actual and then collapse. The role of debit and credit has also explained in which playing with different items like assets, expenses or liabilities which creates creative accounting and increase or decrease profits according to their wants.

Corporate governance can play role to reduce the risks of investors and show true and fair view of financial reporting. There are some choices in current accounting rules under International accounting standards and U.S. GAAP that allow managers some choice in determining methods of measurement and criteria for recognition of various financial reporting elements.

Financial report should be audited by an independent to reduce the information risk and to enhance perceived integrity.

The audit committee of the board comprising of independent non-executive role to prevent misuse of creative accounting techniques and observance of ethical standards in financial reporting. It was explained that it is not that creative accounting solutions are always wrong. It is the intent and the magnitude of the disclosure which determines its true nature and justification.

### Table no. 3- Rewards of the managing Profits (Earnings Management) & Financial Position

<table>
<thead>
<tr>
<th>Category</th>
<th>The Objectives &amp; Benefits Companies Trying To Achieve</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share-Price Effect</td>
<td>Higher Share Price Reduce Share Price Volatility Increase Firm Value Lower Cost of Equity Capital Increased Value of Stock Options</td>
</tr>
<tr>
<td>Borrowing Cost Effects</td>
<td>Improve Credit Rating Lower Borrowing Costs Relaxed or Less Stringent Financial Covenants</td>
</tr>
<tr>
<td>Management Performance Evaluation Effects</td>
<td>Increased Bonuses based on Profits/ Share Price</td>
</tr>
<tr>
<td>Political Cost Effects</td>
<td>Decreased Regulations Avoidance of Higher Taxes</td>
</tr>
</tbody>
</table>

Source: The Financial Number Game by Charles W. Mulford & Eugene E. Comiskey, 2002 (John Wiley & Sons)

Fišerová has explained creative accounting in context of joint stock company that how they show fiction statement than reality to take a loan they show higher value of assets, low profit again at the time of paying tax to the government and again profit increases at the end of the year when information is to be given to shareholders.

Creativity in the accounting comes at a time when it should reach to the public in the form of true background, figures and results. This transforms the actual financial statements to those which the owner would like to achieve as positive and favorable results of the company. It is the shareholder and director who are responsible for the accuracy of accounts. But the paradox remains with the fact that the expert must to find out the accounting and tax levers to fix situation when the enterprise gets into trouble through its creativity. It was also explained that whatever reason whatever is creative accounting will always be reflected in financial indicators and ultimately at the company solvency, bankruptcy, insolvency etc.

Creative accounting could be restricted at so-called harmonization of financial reporting and by application of...
mandatory IFRS (International Financial Reporting Standards) IAS, which are international guidelines for accounting also preparation and presentation of financial statement published by the International Accounting Standard Board (IASB).

Anonymous (1997) has explained what are the economic incentives of creative accounting. Choice of creative accounting is not causes because of performance but the specific characteristics of the company. The relevant economic variable gearing, size and earning volatility are measurable and give predictable results. As more as a geared a company the greater its use of creative policies to increase its reported earnings. Larger organisation and those in monopolistic, or more regulated, industries also have an economic incentives to employ creative accounting. Companies with economic power because of their bigger market size tend to reduced or smoothed profit to avoid the attention of monopoly authorities or costly lobbying by other groups with a political agenda. Companies in the water industries, hotels and leisure and brewing employ more creative accounting techniques than companies in the electricity and financial service industry which employ fewer.

Company’s auditor also play a role to determine the extent of creative accounting use in the company. Research done and found that in big firms also auditors allow creativity. The link between variables such as gearing, size and earnings volatility and accounting policy choices occurs because imperfection in capital markets create a real incentives for companies to adopt creative accounting.

Park (1958) kept different approches to explain the types of thought necessary for developing accounting idea’s principle. what are the thought process in creative accounting and how we organise our thinking.

Creative thinking is necessary for measuring enterprise financial position and operating performance and providing information geared to managerial decision making. Mere technical advancement cannot fill the bill. The impetus for creative development must come in greater measure from thinking generated within the intellectual circle of our own profession. Must creat receptiveness for the innovations and should anticipate the demand for each new informational device and its supporting rationale and educate the users of financial information to their future needs.

Nurturing open minded attitude need creative accountancy research in accountancy. Office and factory are laboratory of accountant. The general theory and technique of accountancy will achieve its brillian through future directed creative effort.

To accomplishment of objectives stated above involves applying scientific method, eliminating logical fallacies and using operational approaches to creativity to solve accountancy's problem and for expanding perimeter of its theory.

Moldovan, Achim & Avram (2010) focused on how information provided by accounting effects external users, and mainly on how and why distorted information gets outside of the organisation into the hands of unsuspecting users. It was also explained there is a inverse casual relationship between true and fair view principal and creative accounting.

“True” and “Fair” cannot be defined easily. Defination given by some authors to this concept, first “true” and “fair”, nither of which are easy to define and secondly there are those who expalin true and fair view in terms of “generally accepted accounting principles rather than accepting the concept as an independent quality”.

True and fair view through financial report’s respect both word of law and its spirit. It is acknowledge that true and fair view expresses the responsibility of company management and auditors to show the correct financial position of the company.

In the anglo-saxon accounting system this principle is valued more than any principles. As using more set of accounting policies overriding for true and fair view which provides accounting choices for different methods. The chances of creative accounting increases. But it depends on intention. If intention is not bad it will give true and fair view of accounting information.

Healy & Wahlen (1999) described about how standard setters should decide or make accounting standards to reduce the possibility of earning management. Information about the comapny is provided by the financial repoting which should show the true and fair view of company but managers manipulate the financial numbers than actual due to their personnel interst like to increase their management compensation, to provide low salary to employees, to pay less dividengs to the sharehoders.

Standard add value if they enable financial stataement to show difference between the relevances and reliability of accounting information under alternative standards.

The chairman of SEC, Arthur Levitt, express worried over earning management and its impact on resource allocation. Some creative accounting techniques noticed like premature revenue recognisation, cookies jar reserves, and write-offs of purchased in-process R&D are threatening the credibility of financial reporting. In this article, reviewers want to find the answer of a central question for standard setters and regulators, therefore, is to decide how much judgement to allow management to exercise in financial reporting.
The standard setters are likely to be interested in evidence on:

- The magnitude and frequency of any earning management,
- Specific accruals and accounting method used to manage earnings,
- Motives for earning management and
- Any resource allocation effects in the economy.

Much of the academic research on earning management is of only limited value to standard setters and regulations. Earning management occurs due to various reasons, including influence market perception, to increase management compensation, to reduce the likelihood of violating lending agreements and to avoid regulations.

Balaciu, Bogdan & Vladu (2009) has done short review of creative accounting topics and its development to know about what are the motivations for creative accounting literature and solution to this creative accounting term. They tried to correlate creative accounting with different interest area like bankruptcies, audit, governance, financial market, the public sector and quality of financial reporting to prevent creative accounting by taking various articles from scientific data source like Science Direct, Emerald, Repec, Google Scholar etc.

4. CONCLUSION

After review articles from various source we can say that creative accounting has many tools to do creative accounting. It increase or decrease profits in company’s favourable enviroment which lead to increase market price of the shares of the companies, reduces tax liability if the company, show higher or lower profit by capitalising expenses and Research & Development expenses. Creative Accounting may leads to land company into crises as history shows in case of Enron and World.com cases, but many time help also to save company from land to crises. It happens because of many loopholes available in the tax law and accounting method eg. Changing Depreciation method from Straight Line to Diminishing Method and FIFO to LIFO methos in case of Inventory. The effect of creative accounting can be minimized by Corporate Governance and fixing ethical behaviour of Auditors.

5. RECOMMENDATION

For improving financial reporting quality and to increase the faith of investors in company’s financial report corporate governance can play a big role in which independent directors can be chosen by the shareholders which works upon the managers activities and keep eyes on managers activities. Because financial reporting is true indicators company’s operating activities and should provide true information to shareholders about the company’s state of affairs. So that investors can take decision to invest in company or not. In that area, independent auditors can be employed to check the state of affairs of the company and give true and quality information to the share holders and stakeholders like creditors bank etc. they should work without any pressure of the management.

Ethics of auditors is also explained in which it was discussed that auditors have some ethics to the society and mangers have also some ethics to not show the manipulated figures but to show true and fair view of the company. Mangers should take responsibility of bad position of the company. Auditors should provide good information to shareholders and check all the transactions and can ask from the managers any suspicious account or dubious transactions. They should provide quality and competent service to their customers. An auditor should be confident, good knowledge of existing law and regulations and he should be updated.

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- [www.proquest.com](http://www.proquest.com)