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PROCEDURES AND TECHNIQUES SPECIFIC TO CREATIVE ACCOUNTING USED IN REGISTERING THE EXCHANGE RATE DIFFERENCES

Case
Study

Keywords

*Creative accounting,
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JEL Classification

M40, M41

Abstract

The purpose of accounting is to show an entity's trusty image through different financial reports. The information provided by these reports are used in the decision making process by different categories of users. Throughout time different procedures and techniques have been developed, through which an „embelishment” of financial reports is made. These procedures and techniques are specific to creative accounting and have the capacity to influence both the profit and loss account, but also the entity's balance sheet. Only by knowing the procedures specific to creative accounting, can the users of financial reports identify the situations, reasons and consequences of their appliance on the information based on which they will make certain decisions. A domain in which the techniques of creative accounting have the capacity of influencing the exercise and implicitly the owned contribution is the one concerning the exchange rate differences.

INTRODUCTION

Economical – financial information resulted from accounting processing are used by different categories of users in the decision making process, both at micro and macro economical levels.

Although the financial information is produced in a legal framework which regulates in a quite precise manner the rules of its presentation, usually it is ascertained that a correction of the result and a legal and legitimate adjustment of the balance sheet is practiced by many entities which take advantage of the versatility of accounting and juridical rules, where the concept of creative accounting derives from. (Cernușca, 2004). In other words, starting from the flexibility of the current accounting regulations, which truthfulness applied, also allow the obtaining of a trusty image, both of the financial position, as well as of the entity's performance, different techniques, procedures and methods have been developed, which brought forth the creative accounting.

A domain in which the techniques of creative accounting have strongly made felt is the one of highlighting the emerged exchange differences, no matter if it is about debts or receivables. Even though, according to the current stipulations the exchange differences have to be acknowledged in the profit and loss account, when they appear, there is an exception concerning the net investments in an external entity. This exception is the one that allowed the creation of certain techniques and methods of the creative accounting in this domain. Conceived and structured based on a complex matter, this paper is considering the presentation of certain elements of creative accounting referring to the exchange differences, as well as a study case which practically reflects the implication of different procedures and techniques of creative accounting in the exchange differences domain, on the accounting registrations of these elements.

METHODOLOGY

The purpose of this scientific approach is the one of presenting both theoretically and practically, certain aspects concerning the situations, reasons, and the consequences of applying the techniques and procedures specific to creative accounting in the exchange differences domain. The methodology we have used in order to achieve this scientific approach, is based on the theoretically research of the concepts of economical – financial information, creative accounting and exchange differences, together with the empirical research through which we have highlighted peculiar aspects concerning the approached concepts. We have appealed to studying researches from the financial and creative accounting field, elaborated by specialists and

theoreticians from this domain, to studying the Accounting Standards, respectively the regulations in this domain, thus being a qualitative exploratory research, and also we have appealed to giving practical aspects specific to different procedures of creative accounting concerning the exchange differences, thus being a quantitative descriptive research.

ASPECTS CONCERNING CREATIVE ACCOUNTING

Creative accounting is consisted of the ensemble of techniques, operations and liberties, left by accounting texts, which without alienating from the norms or from accounting exigencies, gives the entities' leaders the possibility of juggling with the result or to modify the aspect of synthesis accounting documents. (Gillet, 1988).

From another point of view, creative accounting represents a communication technique which aims to ameliorating the information provided to the investors. Taking advantage of the limits of normalizing the accounting we state that through creative accounting the image of financial position and the company's performances is embellished, but we consider this practice as being the limit of legality. (Trotman, 1993).

On the other hand, the creative accounting may be considered as being a consequence of financial engineering, an interpretation of financial creativity. The financial engineering interminably creates new products, which sometimes have as an objective the modifying of accounting or fiscal instructions, and the accounting "technology" which registers these innovations often points out to creative accounting. (Cernușca, 2004).

The opportunities of creative accounting result from: the possibility of choosing among different accounting methods, the estimation tendencies, artificial transactions, planning the authentic transactions. The standard setters who want to keep control of creative accounting, appeal to different solutions, according to the opportunities, as follows: reducing the number of allowed accounting methods, minimizing the chance for estimation, domination of artificial transactions invoking the "substance over form" concept, revaluation prescriptions. (Amat et al, 1999).

The techniques of creative accounting may be classified according to the effects they have on the result or on different posts from the balance sheet:

- the results account and accounting policy: modifying the current result and the net result (amortizations, reserves, stocks, display costs), modifying the current result without influencing the net result, modifying the net result without influencing the current result (investments grants),

accounting taxation and policy (expenses activation).

- the results account and managing decisions: current result amelioration, attenuating or transferring losses), amelioration of net result (lease – back).

- balance sheet amelioration techniques: own capitals (assets revaluation, financial assemblies), permanent loans (leasing), need for working capital and treasury (commerce effect removal). (Cernușca, 2004).

Through creative accounting the numbers may be manipulated so as certain indicators which different categories of users of financial reports are searching for, to have a certain value and implicitly, a certain influence on the decisions made by these.

ASPECTS CONCERNING THE TECHNIQUES OF CREATIVE ACCOUNTING SPECIFIC TO EXCHANGE DIFFERENCES

The entities register both receivables as well as debts, following the realized transactions and operations. Not always these receivables and debts result from operations made in national currency. As a result of the legal obligation of the entities of keeping the accounting in the national currency, these must register the respective elements at their value, in Ron. In order for this thing to be possible, it is appealed to the exchange published by Romanian National Bank.

The exchange rate is volatile; therefore, positive differences appear, which are registered as incomes, but also negative differences, registered as expenses.

According to IAS 21, any exchange difference concerning a receivable or a debt must be acknowledged in the profit and losses account when it takes place, no matter if it is realized or not. Exception for this rule, are the net investments in an external entity. As a result, this rule makes room for subjectivity. (IAS 21, 2013).

Starting from these aspects, creative accounting has developed different techniques and procedures specific to the differences of exchange differences, which refer to:

- if the result influencing is followed, the loan is recognized as being of a defined term, the exchange differences must be accounted for based on the income and expenses account;

- if the result influencing is not followed, the loan is considered to be of an undefined term, and the exchange differences must be accounted based on own capitals. (Cernușca, 2004)

As a result, the techniques of creative accounting specific to the exchange differences have the

capacity to influence the result of financial exercise and implicitly, the tax due.

QUANTITATIVE STUDY CONCERNING PROCEDURES AND TECHNIQUES OF CREATIVE ACCOUNTING REFERRING TO EXCHANGE DIFFERENCES

1. The example entity, S.C. Alfa S.A., Romanian entity, owns a subsidiary abroad. The entity gives its subsidiary, a 18400 Euro as a loan, in 15.10 N, at a exchange rate of 4.4955 Ron/Eur. At the end of the financial exercise, the receivable is evaluated at a exchange rate of 4.5411 Ron/Eur.

Case 1. The entity recognizes the loan as being on a defined term

Receivable evaluation at 31.12 N			
„Long term loans”	=	„Incomes from exchange differences”	839

18400 Euro x (4.5411 Ron/Euro - 4.4955 Ron/Euro) = 839.04 Ron

Considering the loan as being on a defined term, the entity promotes a policy of influencing its results, the exchange differences being accounted for through financial incomes accounts. The entity obtains a favorable image of the result in front of the users of financial information, especially of investors and creditors.

Case 2. The entity recognizes the loan as being on an undefined term

Receivable evaluation at 31.12 N			
„Long term loans”	=	„Incomes from exchange differences”	839

18400 Euro x (4.5411 Ron/Euro - 4.4955 Ron/Euro) = 839.04 Ron

Considering the receivable as being on an undefined term, meaning a permanent financing, the entity does not promote a policy of influencing its results, the exchange differences being accounted for through own capitals account, according to IAS 21.

2. The example entity S.C. Alfa S.A., Romanian entity, owns a subsidiary abroad. The entity borrowed 11200 Euros from its subsidiary at 12.09 N, at a exchange rate of 4.4501 Ron/Eur. At the end of the financial exercise, the debt is evaluated at a exchange rate of 4.5411 Ron/Eur.

Case 1. The entity recognizes the loan as being on an defined term

Receivable evaluation at 31.12 N			
„Expenses from exchange differences”	=	„Loans received from subsidies”	1092

11200 Euro x (4.5411 Ron/Euro - 4.4501 Ron/Euro) = 1092 Ron.

Considering the loan as being on a definite term, the entity promotes a policy of fiscal optimization, thus diminishing the taxable result. The exchange differences are accounted for through financial expenses accounts.

Case 2. The entity recognizes the loan as being on an undefined term

Receivable evaluation at 31.12 N
 „Reserves = „Loans 1092
 from received
 revaluation” from
 subsidies”

11200 Euro x (4.5411 Ron/Euro - 4.4501 Ron/Euro) = 1092 Ron.

Considering the loan as being on an indefinite term, the entity doesn't promote a policy of fiscal optimization, respectively of fiscal optimization. The exchange differences are accounted for through own capitals accounts, according to IAS 21.

3. The example entity S.C. Alfa S.A., Romanian entity has a debt of 23700 Euros to an extern provider, the exchange rate at the date of loaning is 4.3102 Ron/Eur. At the end of financial exercise, the debt is valued at a exchange rate of 4.5411 Ron/Eur.

Case 1. The entity promotes an accounting policy through which backs away from the IAS 21 stipulations, registering the unexecuted exchange differences through conversion differences.

Receivable evaluation at 21.12 N
 23700 Euro x (4.5411 Ron/Euro - 4.3102 Ron/Euro) = 547233 Ron.

As a result of the fact that the exchange rate has registered a drop, following the debt's evaluation at the actual exchange rate, the entity has registered a positive, favorable difference.

According to the accounting policy promoted by the entity, this favorable difference is postponed in the balance sheet, being accounted based on conversion differences.

„Providers” = „Conversion 5472
 differences”

This registration has an effect on the entity's result, this being under valued with the amount of 5472 Ron. Implicitly, the entity will pay lower profit tax. In the N+1 financial exercise, the conversion differences are stomped.

„Providers” = „Conversion 5472
 differences”

Case 2. The entity promotes an accounting policy through which it gets closer to IAS 21 stipulations registering the unexecuted exchange differences through income and expenses accounts, thus reflecting on the profit and loss account.

Receivable evaluation at 31.12 N

23700 Euro x (4.5411 Ron/Euro - 4.3102 Ron/Euro) = 547233 Ron.

As a result of the fact that the exchange rate has registered a drop, following the debt's evaluation at the actual exchange rate, the entity has registered a positive, favorable difference.

According to the accounting policy promoted by the entity, this favorable difference is registered in the balance sheet, respectively in the profit and loss account, being accounted based on the income accounts, namely incomes from exchange rate differences.

„Providers” = „Incomes 5472
 from
 exchange
 rate
 differences”

This registration has an effect on the entity's result, this being influenced by the amount of 5472 Ron. Implicitly, the entity will pay a higher profit tax.

CONCLUSIONS

Starting from the sometimes opposed interests of those who provide and the ones who use the information provided by annual financial reports in decision making, the entities having the purpose of presenting a situation as favorable as possible, and the users trying to find the aspects which are problems for the entity, it has reached the point where the accounting professionals use different legal techniques, which give the possibility of presenting the elements, respectively the entity's situation in a certain way. This approach is possible because of the creative accounting techniques.

The exchange rate differences, be them additional or undercharged, resulted from receivable and loans evaluation at the actual exchange rate, according to the accounting way, have the capacity to influence or not the result of the entity, respectively the tax due.

By enclosing some loans in currency given or received from the abroad subsidies, as being on a determined term, the exchange differences are accounted through the income and expenses accounts, the entity having the possibility to influence its result either by increasing or by decreasing it. In the same time, a policy of fiscal influencing is promoted, because the tax rate is applied to the entity's result. Thus the entity has the possibility of paying a reduced tax.

By enclosing some loans in currency given or received from the abroad subsidies, as being on an undetermined term, the resulted exchange differences are accounted through some accounts belonging to own capitals. In this situation, the entity's result is not influenced anymore, and the

entity does not promote a policy of fiscal influencing.

Only by knowing the techniques of creative accounting, may the users of financial reports identify the situation when these techniques were appealed to, as well as the consequences on the information used in the decision making process.

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