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CREATIVE ACCOUNTING VERSUS RELIABILITY OF ACCOUNTING UNDER THE FINANCIAL CRISIS

1. Information accuracy and reliability of modern accounting

The growing information needs set for the accounting force the need for change in the scope and time horizon of broadcast information. The final result is that the retrospective accountancy gradually becomes prospective accountancy. The subject of description, in addition to the actual facts, are "virtual" business transactions, showing the estimated or future events concerning the company (Gmytrasiewicz, 2007, pp. 118-119). Traditional databases are enriched with intentional estimates and expectations. Accounting procedures are increasingly based on estimation, and the material accuracy and reliability of accounting information recede into the background.

Considering the above, there is some doubt whether the image of a business should be made flexible to reflect the new economic events or in accordance with certain standards which often do not keep pace with the rapidly changing environment (Kamela-Sowińska, 2005, pp. 1960-1963). This is one of the most important dilemmas because the primary task of accounting is to create a fair picture of a unit's activity, presented in the form of financial statements. To secure proper implementation of all accounting functions, the information contained in the report must have a value of high quality. The quality of information reflects a set of characteristics determining the ability to meet the requirements arising from the execution of accounting functions. (Micherda, 2007, p. 3)

One of the most important qualitative characteristics of information generated by accounting is credibility[1] whose degree determines the accuracy and effectiveness of decisions made by their customers. A prerequisite for credibility is the realization of the "true and fair view" principle, that is, faithful and fair reflection of the economic reality (Walińska, 2005, p. 55). However, its practical application encounters a number of restrictions. This is due to the fact that from accounting the useful decision-making information is expected. On the other hand, too much relaxation in the recognition and presentation of specific economic events may contribute to deliberate and unlawful manipulation and, consequently, a distortion of the presented data.

This problem is especially highlighted with relation to financial crises. Numerous scandals and financial and accounting frauds call into question the credibility and reliability of accounting information. It is true that the economic life has been accompanied by accounting fraud since the beginning of accounting[2], but in recent years cases of falsification of accounts were revealed whose financial implications not only weakened the confidence of investors but also were reflected in the spectacular bankruptcies of companies i.e. Enron (63.4 billion USD), WordCom (103.9 billion U.S. dollars), Conesco (52.2 billion U.S. dollars) and others.

Undoubtedly, the issue of counterfeiting accounts can be considered one of the pathologies of a market economy. Globalization and an increased risk of economic decisions, particularly investment, determine the occurrence of this phenomenon on a hitherto unprecedented scale (Wąsowki, 2005, p. 7). They also gave rise to the spread of the term 'creative accounting' in both scientific and colloquial terminology[3] in respect of these unacceptable practices. However, it is doubtful whether, in relation to fraud, counterfeiting and crime, it is appropriate to define these phenomena by the notion of *creative accounting*, if the word 'creativity' has a positive connotation. Certainly, a more accurate description would be "aggressive accounting".

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1 Credibility means that the information provided should be objective, impartial, free of significant errors, complete.

2 The confirmation is provided by works from the sixteenth century, inter alia, by BW Schneicker who in "Zweigach Buchhalten" (1549), included a description of the misconduct and falsification of accounts. However, Pietro A. in his work, "The double bookkeeping" (1586) described cases of falsification of balance sheets (Cebrowska, Jeżowski, 2000, p. 3).

3 The category of "creative accounting" derives from the British environment of accounting. Already in the 90s R. Parker emphasized the frequent use of the financial statements more often to mislead than to inform. B. Elliot, J. Elliot pointed out that "creative accounting" suggested that the information contained in financial statements, prepared by company boards, were more satisfying for themselves than for the shareholders (Surdykowska, 2004, p. 416).

2. Creative accounting – the essence of the problem

Accounting is not a science and in many cases it gives the possibility of different interpretations of specific events. Therefore, in today's businesses, equally important, and perhaps even more important is another feature of accounting which is its creativity. Creativity is the essence of accounting which includes universal and postulative solutions. It also provides the flexibility and the ability to adjust solutions to specific individual activities, creating areas of freedom (Martyniuk, 2007, p. 165).

When doing accounts, business entities are required to comply with the overarching principles of accounting, which are fundamental and inviolable. The law, however, allows for the possibility of alternative solutions and subjective interpretation of reality. As a result, the same wealth resource may be treated[4] or even priced in different ways. This flexibility of regulations is the effect of the implemented concept of "true and fair view" and it is determined, inter alia, by (Martyniuk, 2007, p. 166):

- lack of capacity to anticipate all events that may occur during the operation of the entity (a lack of such a possibility does not allow for their unambiguous regulation);
- financial – accounting regulations, which are a response to changes in the environment (in practice, both problems and ideas for their solution are formed earlier and far ahead of the pace of creating new regulations and the modification of the existing ones);
- difficulties in application of a narrow set of explicit rules, uniform for all units.

Creativity[5] in its basic sense is undoubtedly a positive connotation because it expresses the idea of action, unconventionality. It is a natural, legitimate, creative element allowing for the most genuine and accurate representation of the unit image while taking into account its individual peculiarities. It is above all an expression of activities being a response to situations that are not clearly defined.

Creative accounting reflects the accounting policy based on acknowledging the changes in the subject and responses to them. It is primarily a manifestation of the right to choose where the regulations provide mutually exclusive alternatives and an individual decides on their choice on his own.

Creative accounting is the opposition of formalized accounting. Codification of accounting certainly gives less room to creative accounting. You can even postulate that if there were no accounting regulations in the form of legislation there would not

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4 One example is the economic measures of low unit value which, depending on the accounting policies adopted, can be treated as an asset element or immediately deducted from profit. Adoption of each of these solutions is determined by the balance value of assets and the level of profit.

5 The word creativity comes from the Latin "create" – to create and means creating a positive connotation (Winniczuk, 1997, p. 556).

be creative accounting. Then information generated by accountancy by means of financial reporting would be presented in accordance with the ideas and intentions of the producers, taking into account the particular interests of individuals. (Wąsowski, 2005, p. 13).

All companies use creative accounting to present financial data and to form the best company image. Creative accounting, however, is not based on full discretion and, as it hsd already been pointed out, it has its own framework under the existing legal regulations. However, in the area of accounting we increasingly see not only the creative act but also distortion and fraud. Economic reality, which is far ahead of legal regulations causes that companies themselves have to solve various problems which involves the risk of errors and fraud in the accounting (Brandy, 2005). Especially dangerous is fraudulently accounting[6] being the opposite of creative activities. Its effect is the chaos of information and manipulation of data, depending inter alia, on: tendentious configuring, selection and hiding facts. They are carried out deliberately in order to improve the image of company[7] and are often justified by the managers as beneficial for the company and its shareholders. This is undoubtedly the "dark" side of accounting, which is not an expression of creative, positive thinking. It is the consequence of manipulation of data, which not only take advantage of loopholes in accounting rules, but also go beyond the law. Manipulation is carried out by the use of inappropriate methods of measurement, ignoring the record of events, and inadequate presentation of them in the report.

Abuse, which aims for better presentation of the entity in financial reports than is permitted by the economic parameters, has nothing in common with creative accounting which is an expression of the policy pursued by the accounting firm. In such situations, it is more appropriate to name it as fraud, deceit, or even a crime.

The question thus arises as to why both the theory and practice of creative accounting are identified with a criminal accounting. There is often a negative determination of creative (criminal) accounting. Certainly, this is determined by the fact that accounting, like any legal system is not free from any kind of manipulations. The sources of these practices may be seen in:

- a need to show the financial results expected by the 'market';
- dependence of the premium for the management on the level of profit;
- a desire to increase earnings or hide losses;

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6 According to International Standards on Auditing (ISA) 240, accounting fraud is defined as a deliberate action aimed at improving the corporate image by including falsifying or changing data in documents, the exclusion or omission in the records or documents the effects of the transaction, the presentation of virtual transactions, incorrect application of accounting principles (Karmańska, 2009, pp. 55.63).

7 Among other things, by showing more profit, acknowledging that the benefits which could be caused, inter alia, stability of dividend payments.

- requirements of the parent unit regarding a specific implementation, the minimum return on investment by the subsidiary;
- hiding the financial risk;
- a desire to persuade lenders and trading partners about the reliability of the unit.

As a result of these activities, the concept of creative accounting is increasingly being used in a pejorative sense, in connection with accounting fraud (Bak, 2009, p. 10). Therefore, in order to eliminate these anomalies in terminology which really mislead to reflect these abnormal activities, the term "aggressive accounting" or "criminal accounting" should be adopted and defined.

In conclusion, it must be assumed that the creative accountancy[8] reflects such action, which, without breaking to the rules of law, represent the most desirable, in the circumstances, the company image. They are the result of basing decisions on principles of law upon the most acceptable customs and accounting policy. However, inflating of the financial position and business value of an enterprise and providing a non-existent state of affairs in the way of fraudulent claims, is a sign of aggressive (criminal) accounting[9].

However, doubts emerge whether the deliberate intention of fraud can still be recognized in the accounting system. Very often, the inadequacy of the balance law is to blame for this situation which, on the one hand, formulates the basic principles of bookkeeping, while on the other hand, it gives a lot of freedom in shaping a unit's accounting. However, in practice it is difficult to imagine such formalization of rules that would set out all issues at length, being at the same time suitable for all units. These limitations are mainly due to the diversity of business operations and the specificity of business units. Therefore, the blame for the deplorable practice of accounting whose financial impact is particularly evident in the context of the last economic crisis should not be placed on the accounting system but people who are guided by different objectives. They often take decisions on the selection of certain financial and accounting solutions, not necessarily based on a sense of responsibility and professional ethics.

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8 Adoption, with reference to creative accounting, of the positive colouring, also confirms the position of the Board of the Polish Association of Creativity which scientifically examines the phenomenon of creativity. They question any use of semantic and substantive abuse concerning the category of creativity. Particularly, their practice of criticism concerns the concept of creativity in the context of deception, dishonesty, violation of law. (Schmidt, 2004)

9 Not to be confused with aggressive accounting concerning errors made while conducting of the accounts. By a mistake unintentional irregularities are understood, associated with the operation of accounts and financial statements. An example of such an error is, for instance, incorrect estimation of reserves due to omission of some facts or their incorrect interpretation.

3. Negative creative accounting practices (aggressive accounting)

The economy is a dynamic creation which entails the ability to create attractive market information. This may be done through creative activities based on legal provisions, but also, which is confirmed by cyclically emerging financial crises through the use of ill-conceived 'creative accounting'.

Intentional, deliberate and conscious manipulation, in order to distort the economic reality of the image in the desired direction, is undoubtedly a manifestation of actions aimed at falsifying financial statements. The purpose of these procedures is primarily to present the economic situation of a unit, so that the recipient of information can create a different picture than the facts. The effect of falsification of financial statements is to provide misleading information whose wrong interpretation by the recipient causes that they will make a loss. (Wąsowski, 2005, p. 9) These activities are held mainly by:

- manipulation, falsification or modification of data or source documents on which the accounts are drawn up;
- misinterpretation or deliberate omission of events, transactions and other significant information in the financial statements;
- intentional incorrect application of accounting policies concerning valuation, classification and disclosure.

The practice has developed many ways to manipulate accounting values. An example of aggressive accounting practices, is "removing" the values of some companies. Migration of values is reflected in a decline in the market value of companies. About how many companies lose it (although they show accrual returns and managers take lavish bonuses) is shown, on the one hand, by reports of listed companies, and on the other hand, by data on the salaries of managers. Other ways relate to both categories of consequential manipulation and balance sheet positions, as illustrated in Table 1.

Table 1
Basic tools of counterfeiting of information generated by accounting

Tools	Examples
Manipulation of the income level	revenue recognition, where there is significant uncertainty as to their actual achievement, inclusion in the books of the current revenue period from services to be provided in the future, manipulation of the time of revenue recognition in agreement with the recipients, Recognition as revenue from the sale of that part about which it is known that it will be taken back by the recipient, fictitious revenue recognition in the interim financial statements.
Manipulating the level of costs	activation of inappropriate costs failure to write off as a loss of worthless assets, acceleration of the recognition of future discretionary spending in the burden of the current period, recognition as an expense for the current period of depreciation of costs which should be included in future reporting periods.
Manipulation of financial results	increased profit due to deliberate bringing about outstanding debts, hiding losses from continuing operations by integrating them into the costs of discontinued operations hiding of invoices or unfounded referrals to their partners, solving part of the reserve under the pretext of its overevaluation, acquisition of stocks or items of low value and writing them off as a loss, unjustified creation of a copy updating the amount due from the contractor, showing a fictitious shortage.
Manipulation of components of assets and liabilities.	recognition of revenue and not of liabilities, when the cash was received, failure to disclose certain or contingent liabilities engaging in transactions whose purpose is to "remove" liabilities from the balance sheet.

Source: own study.

Negative accounting practices are associated primarily with the United States. An example is one of the biggest accounting scandals that led to the bankruptcy of the energy corporation Enron in 2001, causing multi-billion dollar losses.[10] In this case, the accountants used the link structure of Enron and its subsidiaries. Often subsidiaries with the status of special purpose entities were created to hide losses or place commitments in them.

[10] Management of the company for several years had been the subject of interest and investigations of tax offices, stock exchange authorities and the courts. The advisory firm Andersen whose employee had participated in the dishonest controlling of Enron documents also suffered financial implications.

Another example of unacceptable accounting practices applies to cable company WordCom, one of the largest telecommunications companies in the world. The Securities Commission (SEC) accused the company executives of manipulating financial results. The company, through fraudulent practices, had been hiding a loss of 3.8 bn dollars over the four quarters of 2001. Their activities included inter alia understating the operating costs through including the cost of renting links from other operators as capital expenditure. Also, the practice of overstatement of provisions was carried out by drawing on reserves for bad debts and mandatory fees.

Aggressive accounting practices were also observed at Xerox. They consisted of the assignment of the current financial result in deferred income, such as fees for renting, leasing.

Presented aggressive accounting practices are among the many that were recorded in the United States. Other examples of aggressive accounting are illustrated in Table 2.

Table 2

Examples of aggressive accounting in corporate America

Company	**Nature of the unacceptable practices**
Adelphia	Concealment of approximately $ 3.1 bn loans and bank guarantees
Lucent Technologies	Incorrect recognition of revenue in the U.S. $ 79 m
Merck	The inclusion in income of approximately $ 12.4 bn by virtue of insurance, which were never received
Rite Aid	Overstated net income by approximately $ 1.6 bn
Halliburton	Incorrect recording of revenues on account of the implementation of construction contracts
Mirant	Overstatement of assets by nearly $ 253 m

Source: own example based on the example Salik (2002)

The effects of negative practices can also be seen on other markets[11], including Poland. Operating in a market economy, the companies accept to their practice both positive and negative "rules of the game market." Economic practice shows that the problem with negative accounting practices does appear, yet to a much lesser extent than in the United States. However, this is not a marginal problem (Zarzecki, 2003). It is confirmed by the conducted study. In Poland, about 12% of the surveyed firms received the opinion with some reservations from a qualified auditor, where an in-

[11] For example, the armaments company Britsh Aerospace, a Dutch sales company Ahold (manipulation of financial results), Italian food group Parmalat (falsification of accounts by showing non-existent assets of around 10 billion. EURO).

creasing share falls to companies with best-organized accounts (in 2001 – 53% are joint stock companies, 46% – limited liability companies). Nearly 40% of reservations about limited companies concerned in those reports overstatement of the value of assets, an incorrect value of liabilities, overstatement of financial results and improper management's assessment of the possibility of continuing the activities of the entity (Moczydłowska, 2005).

Table 3
Polish examples of aggressive accounting practices

Company	Nature of the unacceptable practices
IDM Warsaw	The company belongs to Elektrim, which in 2000 showed a loss of Zl 77.6 m with the asset value of Zl 13 thousand, in 2001 Zl 16.3 m of profit with assets of Zl 1.45 m
Elektrim	Not revealing in the accounts of economic events such as possession of quasi-option sales. Other abnormal operations concerning i.a. principles of accounting fixed-term contracts
ST Group	Overstating the value of assets through artificial accounting operations
PPWK S.A.	In the report for the first half of 2002 the company overstated revenue by Zl 5.4 m.
Impexmetal	Application of procedures of overevaluation and then lowering of reserves. Reserves were established for any possible, even hypothetical expenses, thus lowering the gross profit of Zl 8 m in order to demonstrate the ineffectiveness of the board. The new management obtained their effective action by drawing on part of the reserves, allowing the profit growth of over Zl 7 m.
Bank Millenium (earlier BIG Bank Gdański)	Overstated financial results by not including in the profit and loss account the cost of provisioning reserves for receivables

Source: own study based on the example Gut (2002).

The following examples reflect the techniques of manipulating the economic image of an enterprise, which may be classified as (Kutera, Hołda, Surdykowska, 2006, pp. 36-38, 63):

1. Window dressing treatments, taken before the end of the financial year to improve corporate image, for example, consisting of short-term clearing of assets before the balance date.
2. Income smoothing, intentional smoothing out fluctuations in the level of profits to a level which is, at a given moment, considered to be optimal from the perspective of companies, e.g. by controlling the terms of economic events, so that the appropriate development of earnings or profits in time is possible.
3. Timing based on awarding economic contracts and recording business transactions not at such a time that corresponds to real economic needs, when it is beneficial to obtain special effects in the financial statements.

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Basing the accounting procedures on estimation makes that the material accuracy and reliability of accounting information in some companies' practice recedes into the background. The problem becomes wrongful accounting practices which result in the company's financial image being differrent from reality.

This is particularly noticeable in terms of financial crises. Numerous scandals and financial and accounting fraud call into question the credibility and reliability of accounting information. The subject of many discussions is the issue of “creative accounting”. However, doubts emerge whether in relation to fraud, counterfeiting, crime it is appropriate to define these phenomena by the concept of creative accounting if the word 'creativity' has a positive connotation. Creative accounting should not refer to mistakes, abuses or fraud, since it is the tool of a company's accounting policy. Surely, a more appropriate term for these reprehensible practices is the 'aggressive' (criminal) accounting.

But whatever the terminology, falsification of financial statements may be regarded today as one of the main pathologies of the market economy, which in an era of globalization knows no boundaries. Their effects are reflected in the spectacular downfalls of companies in many countries. Therefore, it is important to identify the causes, mechanisms and methods of forgery. This will not only advance warning of these unacceptable practices, but also deter potential counterfeiters from reproducing patterns of crime (Karmańska, 2009, 1955). An analysis of areas and techniques of poor practice is a source of knowledge enabling the elaboration of instruments to eliminate these practices. Examples of these activities are continuous changes of IFRS and their adjustment to the growing information needs of the environment. However, no provisions are able to eliminate these practices without a decisive element in these matters, which is the ethics of managers, auditors and members of supervisory boards.

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