

# Empirical Research on the Ethics of Creative Accounting

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## *Abstract*

*The issue of ethics in financial accounting arises in the conditions under which it aims to produce an image of reality so that diverse recipients are informed, and which depend on the assessment of the participants. Their ethics play a particular part in finding the truth, however, because they are those who observe, understand, formalize, and, finally, create financial statements which should reflect the reality faithfully. As temptations are considerable, the search for truth, through formalizing a concrete economic reality, is guaranteed only by the professionalism and consciousness of those involved in the accounting of finance. Accounting practices are basic, however, for creative accounting numerous problems occur. Creating accounting does not clearly correspond to its spirit, even though it fulfils statutory requirements, accounting principles, and reporting norms. The creative accounting function for academics, regulators and investors is of great importance in developing and reporting on financial performance in business. The aim of this research is to identify the degree in which employees in accounting firms in Lebanon use creative accounting techniques.*

**Keywords:** *creative accounting, ethics, financial fraud, innovation.*

**JEL classification:** M41, O41.

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## 1. Introduction

Ethics play an essential role in the accounting profession because accounting services are in the public interest, and its quality impacts are directed not just at the undertaking they have been provided for, but particularly to third parties: the state, shareholders, investors and creditors. Facings or data which, for example, are used to mislead a person, might be manipulated in the abuse of ethical rules in accounting, would encourage a person to invest on false excuses or present their shareholders with surreal situations (Remenarić et al., 2018). Consequently, professional behaviour and work have substantial implications for the entire economy, which is why the interaction between the accounting professional as an information provider

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and its user must be regulated by regulatory laws and customized mechanisms (Trifu et al., 2015).

Nevertheless, the existence of an ethical code is not adequate, and the participation of management is also important to ensure that this code is easy to follow as a directive. Awareness of common ethical principles, the ability to maintain an appropriate and impartial perspective regardless of the circumstances is a basis for all stakeholders, partners, and the community to be respected.

Creating accounting is based on flexibility, in some parts, in contrast to the linear and rigid nature of the accounting profession, and the professionals' ethics is designed to say their words in the legislative fields when the standardiser leaves the option, voluntarily or unintentionally, to demonstrate creative activity.

Certain researchers (Tassadaq & Malik, 2015) claim that this design is based on the selection of the best option on a set of norms and guidelines for classifying, recognizing, evaluating, and dealing with items in the financial statements and professional thinking. The negative evolution of creative accounting does have a direct impact on the lack of credibility of accounting information, particularly among investors and financiers (Henderson et al., 2015).

A question of ethics is connected to creativity and innovation in financial reporting. Financial accounting is considered as inflexible, which does not enable inventiveness to be used. However, this fact has been combated in many circumstances where imagination has been established in financial accounts, when distortion of realities becomes a fundamental requirement and can play an essential part. This is why the idea of "creative accounting" was coined to represent the process by which specialists of financial accounting use their skills to manipulate figures (Comandaru et al., 2020). Creative accounting has evolved from the strain put on accounting customers and the need to justify and validate the activity of the organization and lead to them being as interesting as possible. As they constitute the major source of interest for the business on which the evolution largely rests, the urge to impress and entice them has been developed (Akpanuko & Umoren, 2018). In this respect, inventiveness is considered. Creativity in its limitations is a positive quality, but it generally produces a wrong view of the consumer by producing a parallel picture of the truth in the financial statements (Brander et al., 2018).

## **2. Literature review**

Depending on the characteristics of the environment in which it operates, any organization seeks to adapt to the conditions to remain profitable. The creative activity of the financial accounting system most often occurs through a negative aspect of most of the research, and is viewed as a manipulation process for financial accounting information so that the management or even the ownership of the organization influences the economic and financial performance as desired (Saleh et al., 2021). Increasing/decreasing expenditure, income, assets, owner funds, debts, reassignment of assets or liabilities, modification of the information

shown in the Annex may have many ramifications for using creative and inventive financial-accounting procedures and strategies (Rmenarić et al., 2018).

Consequently, daily issues faced by all those involved in financial accounts are the requisite to manipulate the taxes due, the prerequisites for generating information that misinform shareholder in terms of disguise information, and the prerequisites for manipulating certain forecasts of financial accounting information resulting in the gaining of additional sources of finance. From this viewpoint, innovation and creativity are regarded a sifting in financial accounting (Ababneh & Aga, 2019). However, we must ask ourselves why managers choose such techniques. Regarding the views on creative accounting, other perspectives provide a useful technique for solving new accounting difficulties so that the financial situation and performance of the company are presented as accurately as possible (Tassadaq & Malik, 2015). The inventiveness of accountants is also seen as stimulating the development of accounting and implied the economic and social prosperity of the country.

There are several perspectives in the literature to define the concept of creative accounting, starting with the assumption that creative accounting is commonly used to describe the process by which professional accountants use their knowledge to manipulate the data included in the yearly accounts (Yadav, 2014). Several researchers explain creative accounting as a communication tool to improve investor knowledge (Mulford & Comiskey, 2005; Khaneja et al., 2017). Some take advantage of the restrictions of accounting standardisation by innovative accounts, and they understand that it enhances the image of the financial condition and of company performance. In another way, creative accounting can be defined as using certain deficiency or ambiguity as part of accounts to create a certain overview of the financial performance (Vanberg, 2004).

The creative accounting can also be characterized as a series of methods to either modify result levels to maximize or to minimum or to submit financial statements without mutually exclusive results (Amat et al., 1999). The accounting officer has always had account information, and creativity in the precise negative sense of the term does not entail them.

Other authors do not present creative accounting as a negative issue. Considered virtuous, creative accounting also offers accounting with the means of keeping up with increasing market developments and financial product proliferation (Jones, 2010).

***Creative accounting*** can be characterized by two important aspects:

- It requires the use of the creativity of professional accountants to interpret legal, economic, and financial advances, for which, when they emerged, there were no standard accounting answers;
- In accordance with their influence on the financial situation and economic and financial performance of the businesses, the adoption of creative accounting procedures is launched.

Creative accounting is, in our opinion, the result of flexibility in accounting rules, which provide a real image of the financial condition and

performance of the economic entities if they are applied in good faith. However, every accounting information user does have a particular need, does have specific interests, and is frequently employed to meet personal interests at the expense of the public interest in the flexibility afforded by accounting references. Nevertheless, creative accounting has a negative function in the literature because the use is beneficial to certain users of accounting information.

Over the years, several investigations and inquiries have been conducted on creative accounting, with several investigators attempting to define this idea. The subject of creative accounting and motivational variables, in particular, has undergone a global geographic evolution. The authors who investigated these issues have identified the major factors why managers utilize financial engineering: the payment of managers and the costs associated with interest conflicts (Akpanuko & Umoren, 2018; Gupta & Kumar, 2020). A company's management can artificially control its performance so that statistics that conform to an idea of the "projected" results can be reached. Such action is taken by analysing the circumstances of investors and finding two key motives for manipulating results: the desirability of investors to take their shares and the desire to raise the market value of those shares, which impact the way investors see their business. The following definitions of creative accounting can be inferred on the basis of the analysis of specialized literature:

- *The procedure by which accounting information is changed because of infringements and, by using flexibility, the measures and information methods are chosen that allow the transition of summary papers from what managers are interested in.*
- *Process through which operations are organized to provide for the intended accounting result.*

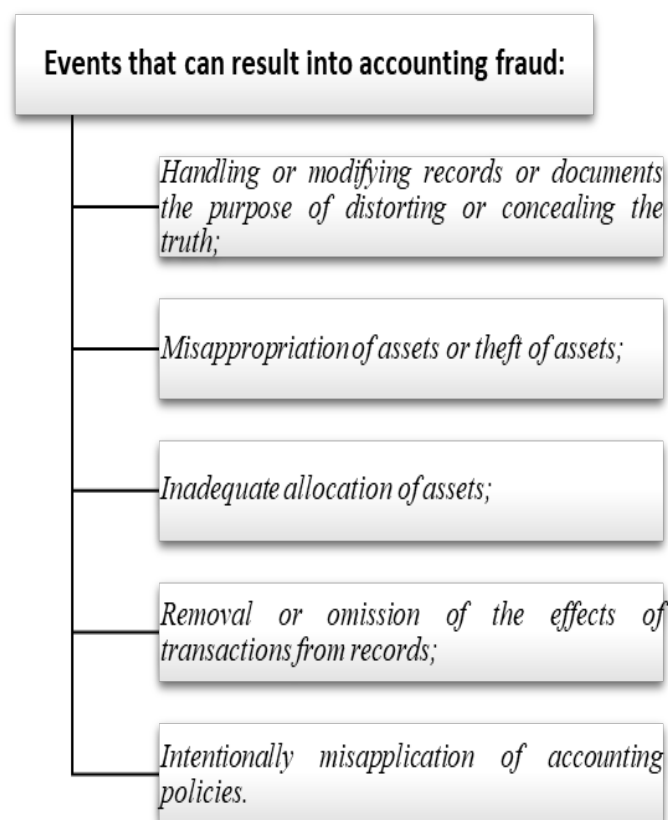
### **3. Creative Accounting versus Accounting Fraud**

Accounting fraud represents a serious act involving frauds to gain an illegal or unfair benefit for one or more people inside the management, those in charge of governance, staff, or third parties (Jones, 2010). In fact, this is extremely difficult to recognize, because it involves the creation of the appearance of normal accounts by utilizing fraudulent papers in order to increase all the costs involved, lower income, keep a record two-fold: true and fictional.

Management is directly connected to the ability to decide on the transmission of the essential information on the correctness of the presentations in financial accounts. Although the management is responsible for preparing the financial statements and the associated information notes, it is not precluded that the auditor makes adjustments in order to obtain the image in question. If management is insistent on a financial position that appears undesirable in the auditor's judgment, the auditor has two options: either to express an unfavourable opinion or to deliver a competent opinion or to reject his audit undertakings (Kouřilová & Plevkova, 2013). Contracting accounts may create a false and distorted view of the economic reality of the business

as a result of violating certain of its accounting principles and rules. This means users' behaviour, the misleading accounting picture, may be changed and can therefore be manipulated by clients. The truth, as is often the case in life, is outside the scope of the auditors who are called on to secure the social credibility of the accounts by attesting that the financial statements depict economic reality according to their adherence to a certain benchmark.

Pressure or incentives to commit fraud could be a cause. This is in the interest of the criminal, in the case of asset theft or an indirect gain in the case of dishonest financial reporting, to gain a direct financial profit. Achieving high profit is the goal of any organization (Deac et al., 2016). The impression of a fraud opportunity among managers is another element that leads managers to utilize accounting fraud. However, the use of deception by managers is not always an opportunity. You only use deception if you believe that you can act without exposure. The term fraud includes deliberate conduct by one or more managers, managers, employees, or others, in order to acquire an unfair or unlawful benefit by using deception a (Zager et al., 2016). The effect of occurrences such as those shown in Figure 1 below may be fraud.



**Figure 1. Actions that can constitute accounting fraud**

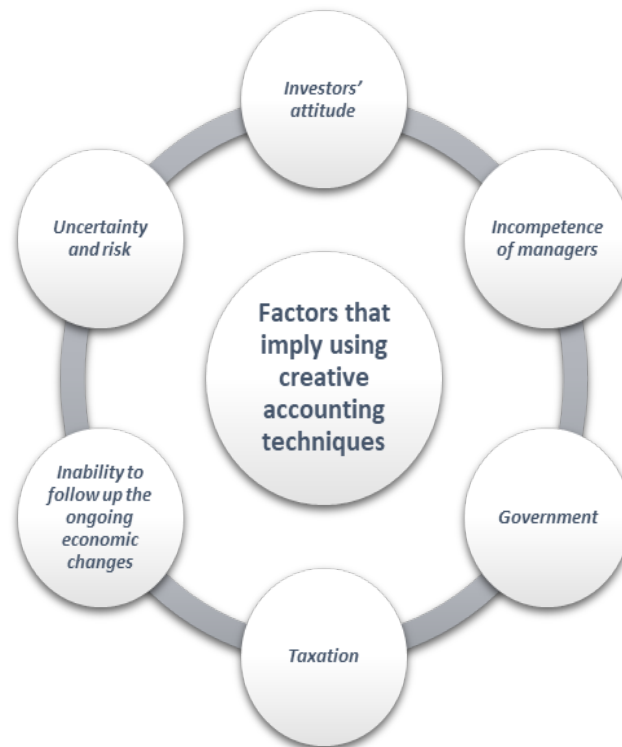
*Source: Authors*

Fraud and creative accountability are therefore not totally synonymous. They are both deliberate measures, but generally creativity, not spirit, follows the law. Creative accounting is lawful; even if used in good faith, it can be a factor in achieving the true picture. However, the use of regulatory loopholes in order to achieve the advantage of certain types of accounting user to the disadvantage of others can be shown to be closer to fraud.

Contrary to fraud, creative accounts use incompleteness exclusively. If the same problem is solved in many treatments, the one that leads to the desired management result is chosen. The practices that do not break accounting rules and cannot thus be fined or prohibited change economic reality, are nevertheless ethically equally repugnant. On the other hand, creative accounting is an essential way to create and portray an accurate image when applied in good faith.

#### 4. Factors that Lead to Creative Accounting Techniques

Considering that financial accounting information is virtually a strategic tool available to managers, it is the first to utilize accounting engineers to market and promote the company's image. The circumstances leading to the need to apply creative accounting technologies are very diverse, as shown in Figure 2.



**Figure 2. Factors that imply the use of creative accounting techniques**

*Source:* Authors

- **Investors' attitude** - Studies have shown that investors often prefer companies with small but stable annual gains. Companies, therefore, have worries over the publication of volatile results with large growth or reduction. The issue of smoothing results comes up, involving the construction and resumption in weak years of unnecessarily large provisions and modifications, where the reported profits are improved.

- **Incompetence of managers** - Incompetent managers rely on special arrangements to the detriment of business prosperity. This damages the company's performance, and the only solution able to cover this problem is creative accounting which can harm links with creditors, consumers, and suppliers.

- **Government** - The government, which provides funds for its effective functioning, is eager to make huge profits in the case of public utilities businesses so it can reduce rates. In this situation, some of these companies are interested in the choice of accounting procedures leading to a reduction in profit.

- **Taxation** - Companies do not like to disclose very large earnings, because the corporation tax debt would grow.

- **Inability to follow up the ongoing economic changes** - Accelerated progress requires a swift pace to identify innovative, information-friendly solutions (Dima, 2021). With normalization in the face of continual delays, the accountant has to develop a creative approach to solve business difficulties in the short term, solutions that do not violate the law, but also favour the company's image.

**Uncertainty and risk** - The usage of creative accounting is motivated by the rise of insecurities due to the fluctuation of the interest rate in connection to inflation and national currency instability.

## 5. Research Methodology

The major purpose of this study is to investigate, through a quantitative investigation, the degree to which personnel in Lebanese accounting companies are using creative accounting procedures. The survey was utilized as the research method in this respect, through the means of a questionnaire. The investigation was carried out in June 2021. The sample consists of 280 employees from 24 Lebanon-based enterprises. The identities of the respondents in the questionnaire have not been requested and the company names are anonymized, so that data confidentiality is guaranteed. In order to investigate the research problem, a set of hypotheses is proposed:

(H1). Men use creative accounting techniques more often in their professional activity than women.

(H2). People with a higher degree of professional training use creative accounting techniques more often.

(H3). Most accountants who have applied creative accounting techniques have encountered positive consequences rather than sanctions.

(H4). There is a correlation between the level of professional training and the belief that innovation and financial-accounting creativity are a fraud.

## 6. Research Findings

According to the answers received, 197 of the total 280 were received complete and valid. This resulted in a response rate of 70.35%. For the graphic illustration of the results, the Office Excel program was used to process the data using the SPSS system.

The initial section of the questionnaire attempted to identify general data on the sample analysed. According to the information gathered and provided in Table 1, the majority of respondents are aged 26-35 (29.44%), followed by 36-45 years (26.90%). The least number of people in the 18-25 category (7.11%) is explained in terms of the nature of the profession of accounting and the fact that prior training and some experience are needed in order to practice. In terms of the subdivision by gender, the sample was found to be statistically representative because of the reasonably balanced ratio of women to men. Thus, the questionnaire was answered by 45.18% of women and 54.82% of men.

**Table 1. Sample distribution by age**

		<b>Percent</b>	<b>Valid Percent</b>	<b>Cumulative percent</b>
<b>Age</b>	18-25 years	7.11	7.11	7.11
	26-35 years	29.44	29.44	36.55
	36-45 years	26.90	26.90	63.45
	46-55 years	19.80	19.80	83.25
	55 or more	16.75	16.75	100.00
	<b>Total</b>	100	100	
<b>Gender</b>	Male	54.82	54.82	54.82
	Female	45.18	45.18	100.00
	<b>Total</b>	100	100	
<b>Level of studies</b>	High School Studies	14.72	14.72	14.72
	University studies	51.27	51.27	65.99
	Postgraduate studies	34.01	34.01	100.00
	<b>Total</b>	100	100	

*Source:* Authors, based on data analysis

Most of the men in the sample reported that they used creative accounting strategies in their business (58.33%) and that fewer than 32% of the women often employ creative accounting approaches in their work (Table 2). According to the data analysis, men employ creative accounting procedures more frequently than women in their work, hence hypothesis 1 is validated.



**Table 2. Gender distribution on usage of creative accounting techniques**

Gender	Have you resorted to the use of creative accounting techniques in your professional activity?				
			Yes, often (%)	Yes, sometimes (%)	No, never (%)
	Male	within gender		58.33	31.48
of total			31.98	17.26	5.58
Female	within gender		28.09	34.83	37.08
	of total		12.69	15.74	16.75

Source: Authors, based on data analysis

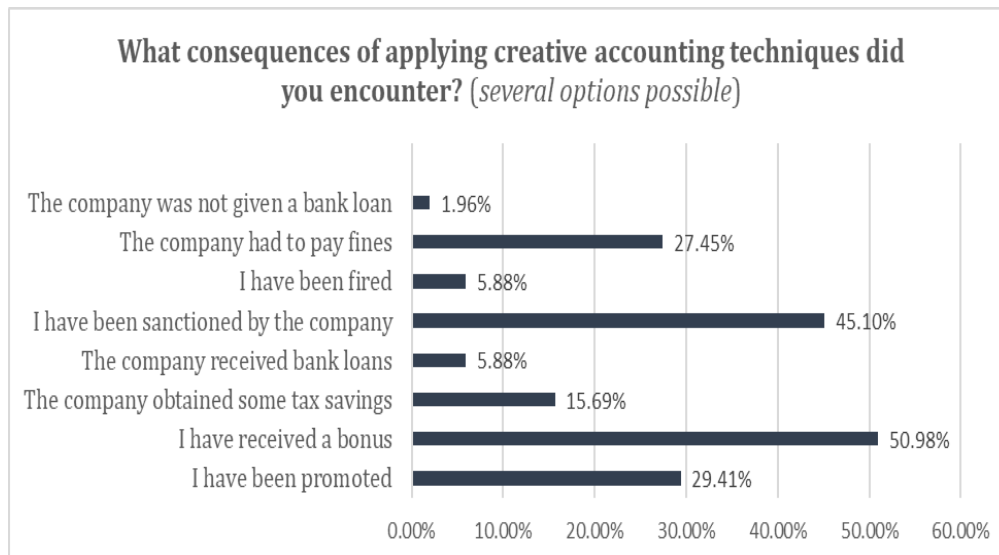
The subsequent analysis included the distribution of the responses about the level of distribution of research on the use of creative accounts. 61.19% of post-graduate accountants frequently use creative accounting approaches, with 56.44% of graduates and 20.69% of secondary students choosing this response option. In addition, 31.03% of high school graduates have indicated that they have never used creative accounting approaches in their business (Table 3). Hypothesis 2 is therefore validated: individuals with a higher professional education employ creative accounting approaches more often than those with a lower education.

**Table 3. Level of studies distribution on usage of creative accounting techniques**

Level of studies	Have you resorted to the use of creative accounting techniques in your professional activity?				
			Yes, often (%)	Yes, sometimes (%)	No, never (%)
	High School Studies	within level of studies		20.69	48.28
of total			3.05	7.11	4.57
University studies	within level of studies		56.44	33.66	9.90
	of total		28.93	17.26	5.08
Postgraduate studies	within level of studies		61.19	17.91	20.90
	of total		20.81	6.09	7.11

Source: Authors, based on data analysis

Most of the respondents believed that it would be advantageous for the organization and for themselves to employ creative accounting procedures. Over half of the individuals included in the survey said those tactics had helped them get a bonus (50.98%) and 29.41 percent said they had been promoted. The main disadvantages faced by the employees were: penalties (45.1%) and corporate fines (27.45%). The results are summarized in Figure 3.



**Figure 3. Consequences of applying creative accounting techniques**

Source: Authors

Creativity and innovation are tied to ethics in financial accounting activities. Many people consider financial accounting to be inflexible and do not allow the imagination to be used. However, this fact is combated by a host of circumstances where imagination can play a very crucial part in financial accounting when distortion of the truth becomes a key requirement. Chi-square testing has been used, showing that there is a correlation between the respondents' level of study and the perception according to which innovation and financial-accounting creativity represent a fraud.

The tests in the Pearson Chi-Square and the Fisher's Exact Test have been considerably lower than 0.05. Pearson Chi-Square and Fisher's Exact Test both have significantly lower values than 0.05 (Table 4).

**Table 4. Chi-Square Tests**

	Value	df	Asymp. Sig. (2-sided)	Exact Sig. (2-sided)	Exact Sig. (1-sided)	Point Probability
Pearson Chi-Square	27.268 <sup>a</sup>	8	.001	.000		
Likelihood Ratio	25.039	8	.002	.003		
Fisher's Exact Test	21.179			.001		
Linear-by-Linear Association	5.394 <sup>b</sup>	1	.020	.023	.012	.005
N of Valid Cases	197					

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a. 12 cells (80.0%) have expected count less than 5. The minimum expected count is .86.

b. The standardized statistic is -2.322.

*Source:* Authors, generated in SPSS

Furthermore, the Nominal Phi is 0,000 and significantly lower than 0,005, confirming the association between the respondents' levels of study and the belief that innovation and originality in financial accounting constitute fraud (Table 5).

**Table 5. Symmetric Measures**

		Value	Asymp. Std. Error <sup>a</sup>	Approx. T <sup>b</sup>	Approx. Sig.	Exact Sig.
Nominal by Nominal	Phi	.731			.001	.000
	Cramer's V	.517			.001	.000
	Contingency Coefficient	.590			.001	.000
Interval by Interval	Pearson's R	-.328	.150	-2.434	.019 <sup>c</sup>	.023
Ordinal by Ordinal	Spearman Correlation	-.267	.159	-1.940	.058 <sup>c</sup>	.058
N of Valid Cases		197				

a. Not assuming the null hypothesis.

b. Using the asymptotic standard error assuming the null hypothesis.

c. Based on normal approximation.

*Source:* Authors, generated in SPSS

Creativity is an issue of perception, usefulness, and ethics rather than an outright infraction of the law. In fact, the image of the financial situation and the company's economic-financial performance is enhanced by the innovative financial accounting activity. In fact, most of the accountants in the research sample share this view. The financial accounting business has a number of challenges that require participants to decide on their actions. Therefore, everyday issues facing all those involved in financial-accounting are the requirements for handling the due duties, requirements for generating certain data that mislead shareholders in terms of hidden information, requirements for manipulating certain projections of the

financial-accounting data that result in obtaining extra finance. Since tremendous temptation is the only thing which can guarantee the quest for truly formalizing a specific economic reality is the professionalism and conscience of those involved in financial accounting.

The summarized conclusions of the formulated hypotheses which form the basis of this research are presented in Table 6 below to analyse the collected data.

**Table 6. Hypothesis analysis**

<b>Hypothesis</b>	<b>Confirmed/Rejected</b>
(H1). Men use creative accounting techniques more often in their professional activity than women.	Confirmed
(H2). People with a higher degree of professional training use creative accounting techniques more often.	Confirmed
(H3). Most accountants who have applied creative accounting techniques have encountered positive consequences rather than sanctions.	Confirmed
(H4). There is a correlation between the level of professional training and the belief that innovation and financial-accounting creativity are a fraud.	Confirmed

*Source:* Authors, based on data analysis

## 7. Conclusions

There are several repercussions in the employment of creative and inventive procedures and policies in financial accounting, including increased/declining expenditure, earnings, assets, owners' funds, debts, reclassification of assets or debts, and the manipulation of the information in the appendix. This statement should affect financial accounting facts, external consumers in particular. The measures taken to stop the use of creative financial accounting practices were not very successful.

By providing fair treatment to all businesses without making any size difference, the State can minimize the temptation of creative accounting. Consequently, firms that have no turnover, overall profitability, or number of employees are not motivated to use methods to categorise them among particular metrics. A fair business reward scheme might also restrict the temptation of creative accounting by omitting or lowering payments. Even as account manipulating takes place with a certain reason, compliance with the norms of accounting must take place. But even if the ethical concept is inadequate, a reward program could attract businesses to offer a realistic picture in order to build a positive image on the market in addition to the financial benefits arising from debt reduction for the state.

To decrease the possibilities of financial engineering, a concept accounting framework to serve as a guide for standardizers should also be developed, respectively, improved in countries where it currently exists. In particular, the conceptual framework provides a mechanism to make normalizers available. It is

also important for professional accountants because it allows them to better comprehend the rules and analyse complex transactions through the criteria it sets.

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