

Креативний облік: дослідження на прикладі готельної галузі Індії

Креативний облік як інструмент розкриття інформації про багатство акціонерів завжди був предметом першорядного інтересу. Протягом багатьох років, такий облік набув різних форм і масштабів використання. Дане дослідження присвячене аналізу практики креативного бухгалтерського обліку в готельній галузі Індії, так як цей сегмент на даний час залишається недостатньо вивченим науковцями. Зокрема, проаналізовано чотири параметри: дискреційні нарахування, індекс маніпуляцій, джерела надходжень та рівень доходів. Результати проведеного дослідження свідчать, що обрані для аналізу індійські компанії готельної галузі в тій чи іншій формі практикують креативний облік. В статті розкриваються рамки можливих рішень стосовно проблеми креативного бухгалтерського обліку. Автор сподівається, що дане дослідження допоможе акціонерам в прийнятті інформації про фінансові результати, представленої компаніями в їх власних інтересах.

Ключові слова: креативний облік, дискреційні нарахування, джерела надходжень, рівень доходів, готельний сектор.

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Креативный учет: исследование на примере гостиничной отрасли Индии

Креативный учет как инструмент раскрытия информации о богатстве акционеров всегда был предметом первостепенного интереса. На протяжении многих лет, такой учет приобрел различные формы и масштабы использования. Данное исследование посвящено анализу практики креативного бухгалтерского учета в гостиничной отрасли Индии, так как этот сегмент в настоящее время остается недостаточно изученным учеными. В частности, проанализированы четыре параметра: дискреционные начисления, индекс манипуляций, источники поступлений и уровень доходов. Результаты проведенного исследования свидетельствуют, что выбранные для анализа индийские компании гостиничной отрасли в той или иной форме практикуют креативный учет. В статье раскрываются рамки возможных решений по проблеме креативного бухгалтерского учета. Автор надеется, что данное исследование поможет акционерам в восприятии информации о финансовых результатах, которая представлена компаниями в их собственных интересах.

Ключевые слова: креативный учет, дискреционные начисления, источники поступлений, уровень доходов, гостиничный сектор.

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Creating Accounting Numbers Using Designed Choices: A Case Study of Indian Hotel Industry

Creative Accounting has always been a subject of prime interest for shareholders' wealth. Over the years, it has diversified into various forms and sizes. The present study contributes by analyzing the creative accounting practices of the select companies in hotel sector in India, untouched so far. It has been analyzed on four parameters: discretionary accruals, manipulation score, quality of earnings and quality of revenue. The results show that these companies do practise creative accounting in one or the other form. The paper concludes with highlighting the scope for possible solutions for the creative accounting problem. It is hoped that the study improves shareholders' perception about the financial results reported by the companies in their self interest.

Keywords: Creative accounting, discretionary accruals, quality of earnings, quality of revenue, hospitality sector.

1. THE PROBLEM

The reality of an enterprise can be mirrored in several aspects, starting from the atmosphere and the environment where the employees perform their daily activity, through the company's brand and to the yearly financial statements. This reality, though, seen from the perspective of the external environment, capitalized in clients, suppliers, public institutions, banks, investors etc, is strongly influenced by the subjectivity of the one watching. This is where creative accounting emerges out.

The informational perspective (Schipper, 1989) is a key element underpinning the study of the creative accounting phenomenon. Managers may choose to exploit their privileged position for private gain, by managing financial reporting disclosures in their own favour. The basis of informational perspective is that that accounting disclosures have an informational signal for the stakeholders.

Creative accounting is a process whereby accountants use their knowledge of accounting rules to manipulate the figures reported in the accounts of a business¹. This practice is carried out with the help of accrual accounting. Goel (2012) study evaluates the implications of discretionary accruals for earnings management in the Indian corporate enterprises. His analysis indicates that there is presence of accrual management in the units.

Authors like (Stolowy and Breton, 2003) are among the few interested in the subject of creative accounting daring to suggest a theoretical framework for the understanding of the accounting manipulation practices. The fundamental principle which their theoretical framework is based on is the following: the aim of publishing financial information is that to reduce the costs of the enterprise projects financing. But this reduction depends on the risks to transfer the riches as they are perceived by the agents on the market. The practical means to operate these transfers are based on the results and the balance between the debts and share capital. Consequently Creative accounting may help maintain or boost the share price both by reducing the apparent levels of borrowing, so making the company appear subject to less risk, and by creating the appearance of a good profit trend.

Creative accounting has emerged as one of the burning issues for regulators and shareholders. The Indian hospitality industry is no exception to it. The **contribution of the present study** lies in the fact that it analyzes creative accounting practices in Indian hotel sector, an area untouched so far. It examines this effect with the help of quality aspect of earnings and revenue which is more relevant from shareholders' perspective.

Hotel Industry in India

Over the last decade and half the mad rush to India for business opportunities has intensified and elevated room rates and occupancy levels in India. Even budget hotels are charging USD 250 per day. The successful

growth story of 'Hotel Industry in India' seconds only to China in Asia Pacific.

With the USD 23 billion software services sector pushing the Indian economy skywards, more and more IT professionals are flocking to Indian metro cities. 'Hotel Industry in India' is set to grow at 15 % a year. This figure will skyrocket in 2010, when Delhi hosts the Commonwealth Games. Already, more than 50 international budget hotel chains are moving into India to stake their turf. Therefore, with opportunities galore the future 'Scenario of Indian Hotel Industry' looks rosy.

2. LITERATURE REVIEW

Conceptual evidences

The concept of creative accounting is usually used to describe the process through which the accounting professionals use their knowledge in order to manipulate the figures included in the annual accounts. Accounting has been defined as 'the art of faking a balance sheet'. Authors like (Stolowy and Breton, 2003) suggested a theoretical framework for the understanding of the accounting manipulation practices. Consequently, the purpose of accounting data management is to change these two measures: the variation of the result per share and the relation liabilities/assets. Creative accounting is used, according to the opinion issued by (Burlacu and Pătroi, 2005) for the 'consolidation' of the economic-financial indicators of the economic entities, distorting yet their informational content.

Historical evidences

The creative accounting appeared in the Anglo-Saxon literature in the 1970s, most often in the papers about the bankruptcy of enterprises and those written by (Watts and Zimmerman 1986, 1990) which represent the foundation of the positive accounting theory. This research trend made the object of several empirical works trying to explain the accounting choices starting from the problem of the political costs that the enterprises are exposed to. More recently, (Brown and Steele, 1999) have selected a portfolio of 12 accounting techniques, combining also the accounting options with the management decisions. In addition to the political costs, it is emphasised the importance of the activity and risk sector and that of the firm operation, as significant determinants of the creative accounting.

From practitioner's perspective, (Jameson, 1988) appreciates the fact that accounting process in its essence, requires the operation with different motivations, different ideas. From this diversity arise manipulation, cheating and falsification at some less scrupulous accounting members. It is he who states that these creative accounting practices do not break the law or the accounting standards; therefore they comply with the law but not its spirit. Jameson states thus the negative character of creative accounting which distorts the enterprise's financial results and the position, misleading the users of the accounting information.

Motivational part

Various research studies have examined the issue of management motivation towards creative accounting behaviour. Half a century ago, (Hepworth, 1953)

¹ *Creative accounting is also referred to also as income smoothing or earnings management.*

identified several motivations including the existence of tax levies based on income, confidence by shareholders and workers in management that is able to report stable earnings and psychological expectations relating to increases or decreases in anticipated income. Tax is mentioned as a significant motivator also by (Niskanen and Keloharju, 2000) in a Finnish context and in Japan by (Herrmann and Inoue, 1996). In countries with highly conservative accounting systems the 'income smoothing' effect can be particularly pronounced because of the high level of provisions that accumulate (Collingwood, 1991) reports on how a change in accounting method boosted a company's quarterly profit figure, by a happy coincidence distracting attention from the company slipping back from being the largest company in the industry in the USA to the number two slot. (Healy, 1985) examines managers' earnings manipulations motives where executive compensation is linked to income measurement.

Remaining on the sphere of serious accounting scandals within the big companies (for example, World Com and Enron) and in the banking sector (for example BCCI, Barings, Allied Irish Bank and Baninter, Mine Omurgonulsen, Ugur Omurgonulsen, 2009) brings into discussion the problem of creative accounting with its legal and illegal facets which occurred on the companies and governments' agenda.

Modeling part

Many research studies examine a particular aspect or technique of creative accounting. All tend towards the conclusion that creative accounting using that particular technique does exist. (McNichols and Wilson, 1988) model the nondiscretionary component of the bad debts provision (so as to identify the discretionary element of the accrual). (Barnea et al., 1976) discuss classificatory smoothing with the use of extraordinary items; their results, based on a study of 62 US companies, indicate that classificatory smoothing does take place. (Black et al., 1998) examine non-current asset sales as creative accounting tools, using a very large dataset of observations from Australia, New Zealand and the UK.

(Lungu et al., 2009) identified the following in their 'not exhaustive census of techniques': (i) manipulation of tangible assets via the practice of 'subjective depreciation' and lease-back arrangements, (ii) goodwill – via underestimation of assets purchased, (iii) depreciation – via using different methods and/or review of useful life of an asset, (iv) inventories – the manipulation of which affects subsequent years, and (v) provisions for liabilities and charges – are used as effective tools for 'leveling' financial outcomes.

(Chen et al., 2012) examine whether different audit procedures and attitudes conveyed to management deter aggressive earnings misstatement that may be fraudulent, and whether such different procedures and attitudes conveyed influence managers' perceptions about the ethicality of any anticipated earnings management.

So, an important differentiation (Jones, 2011) must be made between fair presentation where the flexibility within accounting is used to give a true and fair picture of the accounts; creative accounting where the flexibility

within accounting is used to manage the measurement and presentation of the accounts to serve the interests of preparers.

Gap Areas

The above review clearly indicates that the creative accounting is very fruitful area for academic research in Indian perspective, particularly in a service sector like hotel sector. **Also, most of these studies have analyzed creative accounting with the help of accounting choices, in the form of accruals, exercised by the management. We extend this by examining this effect with the help of quality aspect of earnings and revenue.**

3. OBJECTIVE OF THE STUDY

The study specifically aims at the following:

- To examine the magnitude of discretionary accruals in regard to potential creative accounting.
- To analyze creative accounting with the help of Beneish profit model.
- To explore creative accounting practices further among the units on the basis of quality of earnings and quality of revenue.
- To highlight the major areas of concern in creative accounting in these undertakings for their future viability.

4. RESEARCH METHODOLOGY OF THE STUDY

Following are the main aspects of the research methodology used in the present study:

SAMPLE DESIGN & APPROACH

The present study covers the companies in the hotel sector in India. The enterprises have been chosen on the basis of their performance in terms of revenues and market capitalisation for the period under study. The three leading hotel companies which satisfy the criteria of data availability for the analysis under study are Indian Hotels, EIH Ltd and Hotel Leela Ventures. **Therefore, a 'case study' approach is being followed here.**

Indian Hotels

The Indian Hotels Company (IHCL) better known as the Taj group of Hotels set up in the early twentieth century is one of the largest hotel chains in South Asia.

East India Hotels

EIH Limited is an India-based company engaged in hospitality and related services. The Company operates in two segments: hotels and others.

Hotel Leela Ventures

Hotel Leelaventure Limited is an India-based company engaged in the business of hoteliering. As of August 5, 2009, the Company owned and operated six hotels at Mumbai, Goa, Bangalore, Kovalam (Kerala), Udaipur and Gurgaon.

PERIOD OF THE STUDY

The period to be covered in the present research study is of three years, ranging from 2005-06 to 2007-08. it has been taken as:

- (A) A three year period is reasonably long enough to reveal the short-term and long-term changes and permit the valid conclusions thereof.

(B) Most importantly, this is the period around global recession which itself provides a temptation for creative accounting management.

Therefore, the choice of the research period has not been a matter of an arbitrary decision.

Data used

For the purpose of the present study, the main data used is secondary in nature, keeping in view the nature of the study. the study employs both accounting and market data. the accounting data was obtained from the annual reports of the units and other such records for the relevant period. market data for the units was obtained from the bse site.

Tools / techniques used

The DeAngelo Model

It is considered here for computing discretionary accruals as it provides a direct approach to calculate accruals of discretionary nature, which is more scientific in nature as compared to other models. It is given below.

$$DAC_j = \frac{(TA_{it} - TA_{it-1})}{A_{it-1}}$$

where,

DAC_{it} is discretionary accruals for firm i in period t;

TA_{it} and A_{it-1} are total accruals and total assets for period t and t-1 for firm i.

Beneish Profit model

It has been extensively used in the present study because it provides a comprehensive view of the accruals' analysis with its ratios and the manipulation score. (Beneish, 2011) uses the five financial statement variables designed to capture distortions in financial statement data to assess the probability of detection are:

(a) Day's sales in receivables index - measuring whether changes in receivables are in time with changes in sales.

(b) Gross margin index - assessing whether gross margins have deteriorated, a negative signal about a firm's prospects.

(c) Asset quality index - measuring changes in the risk of assets realization, with an increase to be interpreted as indicating an increased propensity to capitalize and therefore defer costs.

(d) Sales growth index - measuring growth in sales with respect to previous year to find out whether company is adding fake sales.

(e) Total accruals to total assets - measuring the extent to which earnings are cash-based, with high increases in non-cash working capital to reflect possible manipulation.

$$\text{Manipulation Index (y)} = - 4.840 + 0.920*(DSRI) + 0.528*(GMI) + 0.404*(AQI) + 0.892 *(SGI) + 4.670*(TATA)$$

QUALITY OF EARNINGS

Quality of Earnings of the Firm is used, specifically to estimate the extent of creative accounting. *It can be found out by computing the percentage of operating cash flows to net income of a firm.* Higher the quality of earnings, lower the chances of earnings manipulation.

Quality of revenue

Quality of revenue is another important determinant which supports earnings' quality score in regard to determining earnings manipulation. *It can be found out by computing the percentage of collection of sales in cash.* Higher the quality, lesser the chances of earnings manipulation.

5. RESULTS AND DISCUSSION

1 .Magnitude of discretionary accruals

The magnitude of discretionary accruals has been calculated using the De Angelo model for the sample units is given in table 1.

Table 1: Discretionary Accruals

Indian Hotels	2006	2007	2008
Cash Flow from Operating Activities	238.66	520.49	522.96
Earnings before extraordinary Items and discontinued operations	272	474.64	580.47
Total Accrual Adjustments	33.34	-45.85	57.51
Magnitude of discretionary accruals	2.0004	-2.751	3.4506
East India Hotels	2006	2007	2008
Cash Flow from Operating Activities	216.39	186.66	241.19
Earnings before extraordinary Items and discontinued operations	164.69	250.66	349.84
Total Accrual Adjustments	-51.7	64	108.65
Magnitude of discretionary accruals	-3.102	3.84	6.519
Hotel Leela Ventures	2006	2007	2008
Cash Flow from Operating Activities	173.78	227.01	117.69
Earnings before extraordinary Items and discontinued operations	111.54	189.7	223.3
Total Accrual Adjustments	-62.24	-37.31	105.61
Magnitude of discretionary accruals	-3.7344	-2.2386	6.3366

Бухгалтерський облік

The accruals East India Hotels and Hotel Leela Ventures have been increasing over the past three years. This must serve as a potential red flag because not much additions to or removals are being done to property, plant and equipment.

The methodology for estimating Discretionary assets out of total assets is pretty cumbersome. Hence, an estimate percentage related to hospitality sector is made. The trend also shows that both these companies are managing earnings upwards. The Discretionary accruals

of Indian Hotels are swinging upwards and downwards. Hence, it is not following any particular strategy of managing the earnings. Therefore, Indian Hotels may be considered the best among these three Hospitality providers in terms of earnings management.

2. Manipulation Score

The table 2 below shows the above mentioned ratios as well as the manipulation index for the companies.

Table 2: Manipulation Index

(a) Indian Hotels

	2004-05	2005-06	2006-07	2007-08
Sales Growth Index(SGI)		1.405582392	1.382568183	1.121004
Days Sales in Receivables Index(DSRI)		0.955435235	1.103860778	0.905825
Gross Margin Index(GMI)		0.867708611	0.943810371	1.084636
Asset Quality Index(AQI)		1.137906347	1.351786925	0.717095
Total Accruals to Total Assets Index(TATA)		0.050453626	0.033732624	0.000687
Manipulation Score		-1.55373734	-1.38921212	-2.1411

(b) East India Hotels

	2004-05	2005-06	2006-07	2007-08
Sales Growth Index(SGI)		1.433563442	1.199605	1.11932
Days Sales in Receivables Index(DSRI)		0.858844233	0.941507	0.99777
Gross margin Index(GMI)		0.659542317	1.04632	1.031388
Asset Quality Index(AQI)		0.893183153	1.032739	1.13738
Total Accruals to Total Assets Index(TATA)		0.065960855	0.033941	0.015789
Manipulation Score		-1.75400319	-1.77558	-1.84581

(c) Hotel Leela Ventures

	2005-06	2006-07	2007-08
Sales Growth Index(SGI)		1.331664078	1.184668289
Days Sales in Receivables Index(DSRI)		1.149959767	0.75030566
Gross Margin Index(GMI)		0.926787589	1.017211477
Asset Quality Index(AQI)		1.291267879	0.704488419
Total Accruals to Total Assets Index(TATA)		0.118639968	0.03570128
Manipulation Score		-1.02912794	-2.10456872

* Data not available for 2004-05 in case of Hotel Leela Ventures. Hence, score could be calculated for only two years.

In the above analysis, Accrual management in the sample companies was observed on a negative side as expected. All the companies are going for creative accounting on a conservative side, true of a hotel sector. Indian Hotels have been the most conservative among all the units.

3. Earnings' Quality

Earnings quality for the units is analysed as below in table 3 and presented in figure 1.

Table 3: Quality of Earnings

Company	2005-06	2006-07	2007-08	Average
Indian Hotels	142.84%	112.40%	207.88%	121.94%
East India Hotels	136.18%	106.30%	123.35%	121.94%
Hotel Leela Ventures	246.73%	179.30%	79.19%	168.41%

Figure 1: Quality of Earnings trend



As can be seen from the above diagram, the quality of earnings of Hotel Leela Ventures is the highest. Earnings quality here also reflect the sustainability of earnings of Hotel Leela Ventures.

4. Revenue Quality

Revenue quality analysis for the units is discussed below in table 4 and figure 2

Table 4: Quality of Revenue

Company	2005-06	2006-07	2007-08	Average
Indian Hotels	-0.73%	-2.89%	-0.61%	-1.41%
East India Hotels	-2.41%	-1.52%	-1.12%	-1.68%
Hotel Leela Ventures	-1.34%	-2.63%	-0.26%	-1.41%

Figure 2: Quality of Revenue trend



As seen above, the quality of revenue for East India Hotels is the highest. Earnings quality here also reflects the sustainability of revenues of East India Hotels.

6. CONCLUSION

In the present analysis, most of the units have been found to be exercising income-decreasing discretionary accruals, as verified by their negative average. It has been verified by all parameters used for analyzing creative accounting practices in the units under study.

So, the lack of transparency inherent in financial reporting system implies that the potential to misuse it as a powerful tool of earnings manipulation by the management is high, especially where an organizational choice of discretionary accruals to creative earnings exists. So, efforts need to be concentrated on a more deepened analysis of creative accounting and fraud regarding the circumstances which are not known and these elements are worth discussing for investors.

7. LIMITATIONS OF THE STUDY AND IMPLICATIONS FOR FUTURE RESEARCH

There are some limitations of this study which could be categorized as under:

The present study could be confined to only select profit-making corporate enterprises in the hotel industry in India, leaving all other enterprises due to data non-availability. Creative accounting scope can be further examined in other sectors and for other motivational parameters in the light of growing investors' awareness about accrual reported numbers.

The implication for standard-setting bodies is to consider the attributes of assets and liabilities and changes in them also with the fundamental process of measurement of income in the context of creative accounting practices by the corporate.

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