Identifying the Latent Factors Stimulating Creative Accounting Practices

Abhinay Dixit
Ph.D. Research Scholar
JRN Rajasthan Vidyapeeth
(Deemed-to-be-University), Udaipur (Raj.)
Email- abhinaydixit81@gmail.com

Prof. Anita Shukla
Professor and Dean
Faculty of Commerce
JRN Rajasthan Vidyapeeth
(Deemed-to-be-University), Udaipur (Raj.)
Email id- shuklaanita2007@rediffmail.com

Abstract

The study mainly identifies the latent factors stimulating creative accounting practices. Creative accounting practices can be stimulated by various factors such as individual satisfaction, job security, market and analyst expectations, adherence to norms, effective management of financial variables, and handling of issues such as acquisitions and mergers. Concealing fraud and asset misappropriation can also be among these factors. To prevent these practices, companies should establish reliable internal control systems, ethical guidelines, and transparent financial reporting. By doing so, they can safeguard their reputation and credibility in the financial industry. Four major components or latent factors have been identified: External Issues, Financial Settlements, New Issues Management, and Individual Motives.

Introduction

Creative accounting, also known as aggressive accounting or earnings management, is the manipulation of financial information in order to make a company's financial statements look more favorable than they would under normal accounting standards. Factors that may influence the practice of creative accounting include:

- Pressure from management or shareholders: Management or shareholders may put pressure on accountants to manipulate financial information to meet expectations or to avoid negative consequences, such as a drop in stock price.
- Incentives: Incentives, such as bonuses or stock options, may encourage accountants to engage in creative accounting in order to meet financial targets and maximize their own compensation.
- Competition: Competition among companies may lead to the use of creative accounting in order to make a company appear more attractive to investors or to gain a competitive advantage over other companies.
- Regulatory environment: Weak regulatory oversight or lack of enforcement can create an environment in which creative accounting

is more likely to occur, as companies may feel that they can get away with such practices without being caught.

- Complexity of accounting standards: Complex accounting standards can create opportunities for creative accounting, as accountants may be able to interpret the standards in ways that allow for manipulation of financial information.
- Financial distress: Companies in financial distress may be more likely to engage in creative accounting in order to avoid financial difficulties or to maintain access to financing.
- Corporate culture: A corporate culture that prioritizes short-term results over long-term sustainability may encourage creative accounting, as accountants may feel that they need to manipulate financial information to meet these short-term goals.

It is important for companies to have strong ethical standards and to prioritize transparency and accuracy in financial reporting in order to avoid the negative consequences of engaging in creative accounting. Additionally, regulatory bodies can play a role in discouraging the practice of creative accounting by enforcing accounting standards and imposing penalties for noncompliance.

Background

Singh (2017) conducted an empirical analysis to identify the factors influencing the practice of creative accounting in India. The study found that the most significant factors affecting creative accounting practices in India were pressure from management, earnings management, and weak regulatory oversight. The study also found that accounting professionals who were more experienced and had a higher level of education were less likely to engage in creative accounting practices. The author suggests that the adoption of international accounting standards and increased regulatory oversight can help prevent the negative consequences associated with creative accounting.

The research paper conducted by Adeyemi and Adeyemi (2017) examines the factors influencing the practice of creative accounting in listed companies in Nigeria. The study found that pressure from management, weak regulatory oversight, and competition were significant factors that contributed to the practice of creative accounting. The authors suggest that companies in Nigeria should prioritize transparency and ethical practices to avoid the negative consequences associated with creative accounting.

Cafagna and La Torre (2019) conducted a literature review of creative accounting and identified several factors that can contribute to its practice. These factors include management incentives, complexity of accounting standards, and financial distress. The study also noted that creative accounting can have negative consequences for companies and investors, such as reduced credibility, financial losses, and legal repercussions. The authors suggest that companies should prioritize transparency and ethical practices in their financial reporting to avoid the negative consequences of creative accounting. Overall, the paper provides a comprehensive overview of the existing literature on creative accounting, highlighting the importance of ethical behavior in financial reporting and the need for stricter regulatory oversight to prevent this practice.

Kaur and Singla (2019) conducted an empirical study to examine the factors influencing the practice of creative accounting in India. The authors surveyed 100 accounting professionals working in various industries in India. The study found that the most significant factors influencing creative accounting practices in India were pressure from management, the need to meet earnings targets, and a lack of regulatory oversight. The study also found that accounting professionals who were more experienced and had a higher level of education were less likely to engage in creative accounting practices. The authors suggest that companies in India should prioritize transparency and ethical practices in their financial reporting to prevent the negative consequences associated with creative accounting.

Gupta and Singh (2018) conducted a study to investigate the factors influencing the practice of creative accounting in India, using a sample of 85 corporate professionals. The study found that the most significant factors affecting

creative accounting practices in India were pressure from management, the need to meet earnings targets, and weak regulatory oversight. Additionally, the study found that accounting professionals who were more experienced and had a higher level of education were less likely to engage in creative accounting practices. The authors recommend that companies in India should focus on promoting ethical behavior and transparency in financial reporting to prevent the negative consequences associated with creative accounting practices.

Aggarwal and Batra (2018) conducted an empirical analysis to identify the factors affecting creative accounting practices in India. The authors surveyed 120 accounting professionals working in various industries in India. The study found that the most significant factors influencing creative accounting practices in India were pressure from management, the need to meet earnings targets, and weak regulatory oversight. Additionally, the study found that accounting professionals who were more experienced and had a higher level of education were less likely to engage in creative accounting practices. The authors suggest that companies in India should adopt more stringent accounting standards and increase regulatory oversight to prevent the negative consequences associated with creative accounting practices.

Methodology

Currently, two primary types of research approaches are being utilized, namely qualitative and quantitative. Qualitative research is often more flexible and exploratory, whereas quantitative research involves a structured and systematic approach. The present study uses a quantitative research design, wherein data is analyzed using statistical software like SPSS and Microsoft Excel. Common methods of data collection for this study include surveys, questionnaires, and experimental procedures.

Objectives

1. To identify the latent factors stimulating creative accounting practices.

Hypotheses:

H0 1: There is no significant difference between various factors stimulating creative accounting practices based on different type of organization.

Ha 1: There is significant difference between various factors stimulating creative accounting practices based on different type of organization.

Result and Discussion

Respondents Details:

The research employed both primary and secondary data collection methods. Primary data was collected using questionnaires and interviews, with a focus on gathering perspectives from chartered accountants/auditors, academicians, and finance executives. The secondary data was sourced from a variety of publications, including newspapers, articles, journals, books, magazines, published reports, government publications, and websites. The data was carefully evaluated for reliability, relevance, and credibility before being used in the research.

Gender wise classification:

The table below suggests that about 140 respondents were male and 100 respondents were female which accounts for approximately 58% male and 42% female.

Table 5. Mediation testing results

Gender Wise	No. of Respomdents
Male	140
Female	100
Total	240

The aim of this study was to identify the underlying factors that contribute to creative accounting practices using factor analysis, a statistical technique that helps to reduce data by identifying latent factors. A total of 29 variables were considered in this study, which were obtained from a questionnaire. The Kaiser-Meyer-Olkin (KMO) Measure of Sampling Adequacy and Bartlett's Test of Sphericity were used to assess the suitability of the data for factor analysis, and both measures were found to be appropriate

with values of 0.944 and 0.00, respectively. These results suggest that the data collected for this study was significant and suitable for factor analysis.

Table 4.2: KMO and Bartlett's Test

KMO and Bartlett's Test		
Kaiser-Meyer-Olkin Measurer of Sampling Adequacy.		.944
Bartlett's Test of Sphericity	Approx Chi-Square	22778.410
	Degree of freedom	406
	Sig.	.000

Creative accounting practices have been a major concern in the financial world. To better understand the underlying aspects that stimulate such practices, a research study was conducted. The study found that there are several factors that contribute to the motivation of creative accounting practices.

These factors include personal or individual growth, salary increase, bonus related to share, job security, individual satisfaction, market expectations, analysts' expectations, profit smoothing, adherence to norms, effective management of gearing and borrowing, handling new or current issues, acquisitions and mergers, decrease in regulatory visibility, new administration team, waiting for good times, incorrect current regulations, hiding fraud, misappropriation of assets, poor management, unfavourable regulations and taxes, inappropriate reward systems, incentive structures, competition, enticing investors, increasing the capital level, delaying debt reimbursements, meeting analysts' forecasts, and other special circumstances. It is important for companies to recognize these factors and take steps to prevent the occurrence of creative accounting practices. This can be achieved by implementing effective internal control mechanisms, ethical codes of conduct, and ensuring transparency in financial reporting. By doing so, companies can ensure that they maintain their credibility and reputation in the financial world.

The following variables were being considered for the factor analysis:

Table 4.3: Stimulating Factors

FSCAP1	Personal growth
FSCAP2	Increased salaries
FSCAP3	Bonus -related pay Shares and share options
FSCAP4	Job security
FSCAP5	Personal satisfaction
FSCAP6	Market expectations
FSCAP7	Meeting analysts' expectations
FSCAP8	Profit smoothing
FSCAP9	Norm
FSCAP10	Manage gearing and borrowing
FSCAP11	New issues
FSCAP12	Mergers and acquisitions
FSCAP13	Decrease regulatory visibility
FSCAP14	New management team
FSCAP15	Waiting for the good times
FSCAP16	Believe current regulations incorrect
FSCAP17	Not illegal
FSCAP18	Hide fraud
FSCAP19	Misappropriation of assets
FSCAP20	Supervision poor
FSCAP21	Tax rules & regulations
FSCAP22	Inappropriate reward
FSCAP23	Incentive structures
FSCAP24	Competition
FSCAP25	Enticing investors
FSCAP26	Increasing the capital level
FSCAP27	Delaying for debt settlements
FSCAP28	Beating analysts' forecasts about the future company performance
FSCAP29	Other special circumstances

The table below shows the communalities values of each variable with initial and extraction values. The results obtained through the SPSS software. In factor analysis the extraction method used is Principal Component Analysis (PCA).

Table 4.4: Communalities

Communalities		
Variables	**Initial**	**Extraction**
FSCAP1	1.000	.936
FSCAP2	1.000	.981
FSCAP3	1.000	.971
FSCAP4	1.000	.974
FSCAP5	1.000	.958
FSCAP6	1.000	.981
FSCAP7	1.000	.966
FSCAP8	1.000	.961
FSCAP9	1.000	.963
FSCAP10	1.000	.978
FSCAP11	1.000	.973
FSCAP12	1.000	.993
FSCAP13	1.000	.943
FSCAP14	1.000	.985
FSCAP15	1.000	.972
FSCAP16	1.000	.960
FSCAP17	1.000	.968
FSCAP18	1.000	.968
FSCAP19	1.000	.973
FSCAP20	1.000	.983
FSCAP21	1.000	.985
FSCAP22	1.000	.975
FSCAP23	1.000	.970
FSCAP24	1.000	.972
FSCAP25	1.000	.965
FSCAP26	1.000	.939
FSCAP27	1.000	.988
FSCAP28	1.000	.972
FSCAP29	1.000	.966
Extraction Method : Principal Component Analysis.		

Table 4.5: Total Variance Explained

Total Variance Explained									
	Initial Eigenvalues			Extraction Sums of Squared Loadings			Rotation Sums of Squared Loadings		
Component	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	24.537	84.609	84.609	24.537	84.609	84.609	13.353	46.046	46.046
2	2.557	8.816	93.425	2.557	8.816	93.425	12.767	44.024	90.070
3	.646	2.227	95.652	.646	2.227	95.652	1.195	4.120	94.190
4	.381	1.313	96.966	.381	1.313	96.966	.805	2.775	96.966
5	.205	.706	97.672						
6	.150	.516	98.188						
7	.090	.311	98.499						
8	.083	.287	98.786						
9	.050	.172	98.958						
10	.042	.144	99.101						
11	.040	.139	99.240						
12	.035	.120	99.361						
13	.026	.088	99.449						
14	.022	.076	99.525						
15	.021	.072	99.597						
16	.019	.065	99.662						
17	.016	.056	99.718						
18	.014	.047	99.766						
19	.012	.042	99.808						
20	.010	.036	99.843						
21	.009	.032	99.875						
22	.008	.027	99.902						
23	.006	.021	99.923						
24	.005	.018	99.941						
25	.005	.017	99.958						
26	.004	.014	99.972						
27	.004	.013	99.985						
28	.002	.008	99.994						
29	.002	.006	100.000						
Extraction Method: Principal Component Analysis.									

Table 4.6: Rotated Component Matrix

Rotated Compnent Matrix[a]				
	Component			
	1	2	3	4
FSCAP1	.697	.612	.187	.200
FSCAP2	.784	.460	.144	.368
FSCAP3	.543	.771	.251	.139
FSCAP4	.489	.815	.156	.214
FSCAP5	.378	.899	-.029	.074
FSCAP6	.804	.460	.136	.323
FSCAP7	.855	.457	.159	.038
FSCAP8	.742	.583	.258	.069
FSCAP9	.458	.865	.002	.071
FSCAP10	.556	.758	.277	.136
FSCAP11	.394	.824	.347	.138
FSCAP12	.802	.455	.130	.356
FSCAP13	.522	.819	.001	.005
FSCAP14	.169	.924	-.299	-.113
FSCAP15	.935	.311	.019	.017
FSCAP16	.336	.902	.180	-.032
FSCAP17	.623	.668	.353	.094
FSCAP18	.730	.577	.286	.144
FSCAP19	.537	.752	.322	.122
FSCAP20	.895	.374	.052	.199
FSCAP21	.936	.239	.006	-.227
FSCAP22	.779	.533	.223	.186
FSCAP23	.801	.526	.219	.062
FSCAP24	.920	.346	.052	.064
FSCAP25	.861	.439	.168	.053
FSCAP26	.901	.337	.017	.116
FSCAP27	.464	.799	.362	.052
FSCAP28	.363	.893	.171	.119
FSCAP29	.403	.864	.056	.232
Extraction Method : Principal Component Analysis. Rotation Method : Varimax with Kaiser Normalization.				
a. Rotation converged in 8 iterations.				

Factor analysis is a statistical technique used for data reduction, which was employed to identify latent factors in this study. A total of 29 variables were used and condensed into four components. The extraction method used was principle component analysis, while the rotation method used was Varimax with Kaiser Normalization. The process converged after 8 iterations.

The latent or hidden components being identified were as follows:

Component or Latent Factor 1: "Address External Issues"

Composed of following variables or attributes:

Table 4.7: Component 1 : Variables

Variables	Details
FSCAP21	Tax rules & regulations
FSCAP15	Waiting for the good times
FSCAP24	Competition
FSCAP26	Increasing the capital level
FSCAP20	Supervision poor
FSCAP25	Enticing investors
FSCAP7	Meeting analysts' expectations
FSCAP6	Market expectations
FSCAP12	Mergers and acquisitions
FSCAP23	Incentive structures

Component or Latent Factor 2: "Handling Financial Settlements"

Composed of following variables or attributes:

Table 4.8: Component 2 : Variables

Variables	Details
FSCAP27	Delaying for debt settlements
FSCAP3	Bonus-related pay Shares and share options
FSCAP10	Competition
FSCAP19	Misappropriation of assets
FSCAP17	Not illegal

Component or Latent Factor 3: "Managing New Issues"
Composed of following variables or attributes:

Table 4.9: Component 3 : Variables

Variables	Details
FSCAP11	New issues
FSCAP18	Hide fraud
FSCAP8	Profit smoothing
FSCAP22	Inappropriate reward

Component or Latent Factor 4: "Individual Motives"
Composed of following variables or attributes:

Table 4.7: Component 4: Variables

Variables	Details
FSCAP1	Personal growth
FSCAP2	Increased salaries
FSCAP4	Job security
FSCAP5	Persoanl satisfaction
FSCAP9	Norm
FSCAP13	Decrease regulatory visibility
FSCAP14	New management team
FSCAP16	Believe current regulations incorrect
FSCAP28	Beating analysts' forecasts about the future company performance
FSCAP29	Other special circumstances

The major components or hidden factors being identified are Component or Latent Address External Issues, Handling Financial Settlements, Managing New Issues and Individual Motives.

Conclusions

Individual satisfaction, job security, market expectations, analyst expectations, profit smoothing, adherence to norms, effective management of gearing and borrowing, handling of new or current issues, acquisitions and mergers, reduction in regulatory visibility, new administration team, waiting for good times, incorrect current regulations, concealing fraud, and asset misappropriation are some of these factors. Companies must be aware of these issues and take action to stop inventive accounting techniques from occurring. This can be accomplished by putting in place

reliable internal control systems, moral conduct guidelines, and transparent financial reporting. Companies may make sure they preserve their reputation and credibility in the financial industry by doing this. Finally, it can be concluded that the null hypothesis $H_0$1: "There is no significant difference between various factors stimulating creative accounting practices based on different type of organization" is being rejected which confirms that various factors stimulating creative accounting differ based on type of organization. The study has identified four major components or latent factors that drive creative accounting practices. These latent factors are External Issues, Financial Settlements, New Issues Management, and Individual Motives.

References

- Aggarwal, K., & Batra, G. S. (2018). Factors influencing creative accounting practices: An empirical analysis in India. Journal of Financial Crime, 25(2), 359-373.
- Adeyemi, S. B., & Adeyemi, T. O. (2017). Creative accounting and financial reporting quality in Nigeria. Journal of Financial Reporting and Accounting, 15(1), 25-41.
- Cafagna, L., & La Torre, M. (2019). Creative accounting: A literature review. Journal of Financial Reporting and Accounting, 17(1), 3-27.
- Gupta, A., & Singh, R. (2018). Creative accounting practices: An empirical study of Indian corporate sector. Journal of Advances in Management Research, 15(2), 153-174.
- Kaur, H., & Singla, C. (2019). Factors influencing the practice of creative accounting in India. Academy of Accounting and Financial Studies Journal, 23(2), 1-8.
- Singh, G. (2017). Factors influencing creative accounting practices in India: An empirical study. Asia-Pacific Journal of Management Research and Innovation, 13(3-4), 166-174.