



LIBERTY AND CONCORDANCE IN BOOK-KEEPING

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Abstract

The general objective of the paper is to formalize a speech with a theoretical and practical purpose concerning the options of accountancy policies in conditions of regulation, standards, compliance, convergences, harmonisations and professional liberties.

Key words:

IAS, IFRS,
relevance, accounting

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M40; M41

1. Prolegomena for the accounting truth

Liberty and concordance, they both represent an equation of relevance and credibility of the information presented in the financial situations. **Relevance** meaning the supply of predictive and retrodictive knowledge when taking efficient economic decisions regarding the financial position and the performance of an accounting entity, **the credibility** in its turn, the information lacking in significant errors, does not take sides and the users can rely on the fact that what is meant to be represented is correctly represented or what is expected to be reasonably represented.

Where there are relevance and credibility, a problem occurs: **is the book-keeping capable to put forward a truth and an objective truth.** The idea and the formulation are excessively categorical and unjustly generalizing, even if we can bring as a support the scientific authority of the French Professor A. Cibert who affirms: „There are as many truths as consignees of the information and in the measure in which it excludes the quality, the reductive effect of each measure is inevitable.” And to be more persuasive, he appeals to P.Lasseque, B.Colasse and D.Boussard who admit in their turn that the **<truth>expressed by the book-keeping is only a filter which allows the understanding of a reality. Though, due to its internal coherence that gives strength and at the same time weakness, the book-keeping permits to reach a formal truth based on several postulated conventions, norms, rules of classification.**

When asking the question „Is there any accounting truth?” we can answer as Pirandello would have answered „**Everyone with his own truth**”. Consequently, being a stake for different social

protagonists, the truth, being rendered by the faithful image of the financial position and performance, must be sought for depending on the interests of the producers and users of information.

The truth supplied by the book-keeping cannot be for the users but the result of a compromise between expectations and exactingness, and for the producers, a report between sincerity and regularity (the respecting of the principles and the fundamental rules).

Respecting the accounting truth, we present the **“Contents of the accounting liberties”** which can have the following classification:

- The application of the options connected to the permitted accounting politics, base treatments and alternatives
- The preferential application of the evaluations in book-keeping
 - The depreciation test of the assets
 - The reevaluation of the lock-up
 - The change of the evaluation methods of the inventory
 - The subjective evaluation of the un-bodily lock-ups and financial titles
 - The modification of the writing-off rhythm
 - The flexibility of the politics regarding the allowances
 - The internal prices of abandonment of the assets and those of abandonment between the branches of the same group
- The manipulation of the accounts by structuring and postponing the real transactions

- The increase of the difference between the accounting registering value and the acquisition price by underestimating the bought asset and the imputation of the differences upon the reserves
- The realization of lease-back operations through which the sale of an active is made followed by its renting from the buyer enterprise.
- The attenuation of the claim losses by underwriting an assurance, having as effect the improvement of the result with the difference between the value of the claim depreciation and the premium paid.
- The issue of hybrid titles through which the firms can transform some debts in personal capitals
- The transfer of some assets to another firm, together with the management of the debt, operation named „the annulations of the fact obligation”.
- Aggressive and cautious accounting treatments regarding the incomes and the expenses. The constitution of the desired performance
- Accounting treatments regarding the value depreciations and increase. Aggressive and conservatory. Incertitude and risks. Backing book-keeping
- Liberties and accounting options regarding the maintenance of the capital. The evaluation basis. The recuperation of the historical cost and the maintenance of the nominal value of the financial capital. The price of money in time.
- Accounting liberties regarding the sweet marriage of the fiscality and book-keeping. The commercial book-keeping and the fiscal book-keeping; the financial book-keeping and the business book-keeping; the management book-keeping and the costs book-keeping
- The opening and the multiplications of the accounting liberties regarding the presentation of the information; the financial analysis and the interpretation of the financial reports with general purposes. The passage from numerical information to narrative information. The ad-interim information and the foreseeable information.

2. Liberty and concordance in a normalized/settled book-keeping

Appealing to IAS 1 “The presentation of the financial situations” the equation of the accounting concordance and liberties can have the following form: *concordance + liberty = concordance with something*

pre-established + the possibility to depart from the relevant frame of settlement + supplementary information + the professional reasoning when selecting the accounting politics.

„An entity whose financial situations are concordant with the IFRS must present in notes an explicit declaration and without any reservations regarding this concordance. An entity will not describe the financial situations as concordant to the IFRS only if they satisfy all the IFRS dispositions.”

In almost all the situations, an entity realizes a faithful presentation by respecting the applicable IFRS. Also, a faithful presentation imposes to an entity:

(a) To select and to apply the accounting politics according to IAS 8 “Accounting politics, modifications in the accounting estimations and errors”. IAS 8 establishes a hierarchy of guidance having a norm value which is taken into consideration by the management in the absence of an IFRS that is normally applied to an element.

(b) to present information including the accounting politics in a manner that offers relevant, credible, comparable and intelligible information

(c) to offer supplementary information when the respecting of some IFRS dispositions is insufficient to permit the users to understand the impact of some transactions, of other events and conditions upon the financial position and financial performance of the entity

An entity cannot rectify the inappropriate accounting politics through the used accounting politics or through notes or explanatory materials.

In the extremely rare cases in which the management reaches the conclusion that the respecting of an IFRS disposition would mislead so much that it would be in contradiction with the objective of the financial situations established in the *General frame*, the entity would abbot from that respective task if that relevant frame of settlement foresaw such a deviation or it did not interdict it in another way. (Takeover from IAS 1 “The presentation of the financial situation”).

3. Liberty and concordance in a diversity of accounting politics

The man oeuvre liberty in the formulation of the accounting politics and the choice of the accounting methods although appreciated positively under the aspect of creativity, have always represented a source of controversies regarding the construction and the acceptance of the accounting truth. And as different methods lead to different results, in many turns IASB recognized the necessity of diminishing the possibility of the usage of the alternative treatments allowed to assure a real harmonization.

Liberty and concordance in a diversity of accounting politics become action by appeal to IAS 8 „Accounting politics, modifications in the accounting estimations and errors.” In this way the standard establishes the criteria of selection and application of the accounting politics.

The specific criterion of selection is that of the standard or of the interpretation which is applied specifically to a transaction, to an event or to another condition. In the absence of a standard or of an interpretation which is applied specifically to an element, the management must practice the professional reasoning for the elaboration and the application of an accounting politics that has as result information that is:

(a) Relevant for the necessities of the users of taking economic decisions; and

(b) Reliable, meaning that the financial situations:

- reflect exactly the financial position, the financial performance and the treasury
- flows of the entity;
- reflect the economic fund of the transactions, of other events and conditions,
- not only the juridical form;
- are neutral, meaning lacking in influence;
- are prudent and
- are complete from all the significant points of view.

When practicing the reasoning presented above, the management must refer to and take into consideration the applicable feature of the following sources in a decreasing order:

(a) The dispositions and the guidance from the standards and interpretations that treat similar and connected aspects; and

(b) The definitions, criteria of recognition and the concepts of evaluating the assets, the debts and the incomes and the expenses in the *General frame*.

When practicing the reasoning presented above, the management can take into consideration the most recent norms of other body of standardization that uses a similar conceptual general frame to elaborate the accounting standards, other accounting domains and the practices accepted part of the activity domain, in the measure in which these are not in contradiction with the sources mentioned previously.

The consistency of the accounting politics. An entity must select and apply its accounting politics consistently for transactions, other events and similar conditions, excepting the case when a standard or an

interpretation stipulates or permits, specifically, the classification of the elements for which it could be appropriated the application of some different standard politics. If a standard or an interpretation stipulates or permits such a classification, an appropriate accounting politics must be selected and applied consistently to each category.

Where there is concordance and liberty in the selection and the application of the accounting politics **the transparency and the responsibility** cannot lack.

As we can notice from the accounting standards, the transparency refers to the principle of the creation of an environment in which the information regarding the existent conditions, decisions and actions is accessible, visible and intelligible for all the participants on the market. The presentation of the information refers to the process and the methodology of supplying the information and to the fact that the politics decisions are presented to the public with sincerity and through an opportune spread.

4. The significance limit and the professional reasoning

The relevance of the information is influenced equally by the nature and the significance limit of the respective information. In some cases, the nature of the information is sufficient by itself to determine its relevance. In other cases, both the nature and the signification limit are important.

The information is significant if the omission or their erroneous declaration could influence the economical decisions of the users. The significance limit depends on the size of the element or of the error, judged in the specific environment of the omission or of the erroneous declaration.

The signification limit is an expression of the relativity of the importance and size of some particular aspects in the context of the financial situations as a whole. Thus, **quantitatively**, errors implying sums under the limit of signification must be taken into consideration if there is a risk to be repeated and in the case in which, adding all these sums, a sum over the limit of significance could result. **Qualitatively**, the limit of signification must be considered for example in the case of the presentation of the accounting politics in the explanatory notes of the financial situations, when an incorrect or incomplete presentation can lead to erroneous interpretations of these politics.

Often, the significance limit is calculated as we present below or considering an average/ their mean average : gross profit 0,5-1; sales figure 0,5 -1, total assets 1-2, net active 2-5, profit after taxation 5-10. The significance limit must be periodically revised.

The tolerable error is often calculated as being 75% or even 50% from the significance frame.

Where there is liberty and concordance the **professional reasoning** must be also present. Its density differs depending on the two general characteristics of the accounting systems, respectively **book-keeping based on rules** and book-keeping based on principles. Thus, in the case of the accounting systems based on strict rules, such as USGAAP little professional interpretation of the practitioners are permitted. Plus, in this case, the accounting settlements suffer permanent modifications due to the influences of the business and political environment. The accounting system type IFRS is based on principles that lead to accounting politics according to the stipulations of the standards, but also to the professional reasoning of the practitioners.

Everybody agrees with a system based on principles, but everyone wants rules in order to avoid uncertainties and a second interpretation of the settlement bodies. The principles demand reasoning, and reasoning is a constitutive part of drawing up the financial situations. It is the obligation of those who draw out the financial situations, of the financial directors to realize strong management reasonings. The auditors also must appeal at reasoning, at the evaluation of the respecting of the accounting systems. The need of certitude and uniformity of the financial situations leads to more rules: rules within a company in order to insure the uniform application of the accounting politics, rules within an audit firm, rules within the auditors within a country, rules established by settlement bodies and by governments and, finally, the idea of uniformity at global level. The accountants are in the middle of a triangle, they must evaluate the management reasoning, to apply their own professional reasoning and they will be judged by the settlement bodies, by the public and by the investors. They take over the challenge and the processes and the implementation procedures to assure the uniformity of the standards application. What we want to emphasize is *that we do not have an easy life having rules, and that we will all have to work with principles. IASB is the only body that has to establish the standards in an appropriate way. And this thing requires the application of reasoning.*

And however the harsh attempt for the classification of the book-keeping in **the book-keeping based on principles** and **the book-keeping based on rules** (norms and settlements) is not founded. In this regard, to create the opposition, a book-keeping based on principles and respectively a book-keeping based on rules, signifies to deny the formalism proper to the accounting informational system. The accounting must be simultaneous normative (regulatory), **meaning what one should see** (see the norms), positive, **meaning what it is in fact** (see the specific practices) and

constructive, **what it isn't** (see the synchronic and the diachronic). And if we have doubts about such a book-keeping, we remain with the solution of passing from the **commitment book-keeping to the treasury book-keeping**. The manipulation of the information and treatments does not belong to the treasury book-keeping. And if someone desires a commitment book-keeping, the way from the treasury one to that of commitments is made incidentally.

The intervention in time of the ex president of the USA, mister **George W. Bush** after the acknowledge of the ENRON disaster is significant, especially when he stated 10 proposals regarding the protection of the shareholders and the prevention of the collapse of other societies, the ideas mentioned being focused on three fundamental directions, as:

- correct financial reports, in which the financial position and the performance as well as the risks cannot be omitted.
- the increase of the managers' responsibility, the promptness and the sincerity of the financial declarations
- the investors, the shareholders must have full trust in the independence, integrity and ethic of the financial auditors; the development of a strong competent and independent audit system.

Business men- the President declares- must respond not only to the demands of the market or to personal interest, but also to the emergences of the conscience...and the auditors must compare their clients' book-keeping with the „**good practices**” and **not only with the stipulations of the book-keeping standards**. The spectrum seems more annoying taking into consideration that fraud, according to local professional seems to have been in concordance with the stipulations of the USGAAP. Another feature, **fraud has nothing creative**, being illegal, the option have always existed, no matter if a book-keeping has based on principles or rules, **Achilles' heel** remains the inherent subjectivity of the evaluation, which cannot be omitted. Altogether, we add to the flexibility of the weaknesses connected to the evaluation the flexibility of the options connected with the application of the accounting politics.

5. Aggressiveness and conservatism, prudence and non-prudence in measuring and evaluating the accounting result

The specific accountant theory and practices, as Hennie Van Greuning shows in the book „*International standards of financial report, practical guide*”, second edition revised, appeared in the Irecson Publishing House, Bucharest, 2007, „are generators of aggressive and conservatory in the evaluation of the

gains..The more aggressive the accounting methods are, the lower is the quality of the gains; the lower is the quality of the gains, the higher the evaluated risk is; the higher the evaluated risk is the lower the values of the analyzed society is. (pag. 55).

Elements of the financial situations	Aggressive treatment (it is subjected to the IFRS intention)	Conservatory treatment
Incomes from current activities	Aggressive commitments	Installment sales or the recuperation of the costs
Stocks	FIFO-IFRS treatment	LIFO (where it is permitted – no longer permitted by the IFRS)

Liquidation	Linear (usually according to IFRS)having a higher residual value	Accelerated liquidation methods
Guarantees and uncertain claims	High value estimations	Lower value estimations
Liquidation period	Higher or increasing	Lower or decreasing

This being the situation the problem **principle-criterion** is raised, capable of deciding the choice of the method of the profile construction. The truth in this sense at the present time is based on **the principle of prudence**. As it can be observed in the General frame IASB, *“prudence represents the inclusion of a caution degree in the practice of the necessary reasoning in order to make the estimations demanded in conditions of uncertainty, so that the assets and the incomes are not over evaluated and the debts under evaluated.”* Though, the practice of prudence does not allow for example the constitution of hidden supplies or excessive commissions, the deliberate under evaluation of the assets or incomes, nor the deliberate under evaluation of the debts and expenses, because the financial situations would not be neutral and this is why they would not have the quality of being credible.

Though, for the book-keeping in conditions of liberty and concordance the interpretation: “where is the measure and the lack of measure in the application of the prudence demands in the terms formulated above?” appears. Altogether, for a modern book-keeping, in its quality of measurement instrument but also informational instrument, and especially that of

instrument of social mediation at the present time, in the conception of some authors, *prudence is no longer obligatory a virtue, and the evaluation is treated as a problem of accuracy.* The sum evaluated in monetary unities must represent the best estimation of the assets and debts. The inherent risks and the uncertainties must be taken into consideration in the evaluation methods. At the same time, the law of change imposes the permanent bringing up-to-date by appealing to the fair value and to the recovery value of the assets and debts.

In a more general analysis, it is appreciated that the principle treats discriminatory the evaluation of the assets. According to the principle of prudence, only the depreciation and the value losses of the assets are accounted for, calculated as a difference between the inventory value (actual) and the historical cost but not the capital gains. The lack of registration of the capital gains generates latent or hidden reserves. Also, the hidden reserves can be created through the deliberate under evaluation of the assets or of the incomes or the deliberate over evaluation of the expenses.

In what concerns the evaluation of the uncertainties in book-keeping, meaning the realization of commissions, as Hendriksen E.S. showed, *the principle of prudence is „at best a very middling method to treat existences to uncertainty in the evaluation of the assets, debts and results. The worse, it stimulates a complete distortion of accountant figures. It is extremely dangerous by its capricious effects. As a consequence, accountant figures established prudently do not permit a correct interpretation”.*

The virtues of the principle of evaluation lose their value in the estimation in the monetary unities of the size of the assets, debts, personal capitals, incomes and expenses, in the adoption of the concept of **fair value** within the accountant standards for the draw-up of the financial situations. In the basis of this concept, the assets and debts owned by an entity are evaluated at fair value, generators of recognized pluses /minuses, recognized by the case, as result elements or as personal capitals elements.

Although it is objective and reliable and is in no need of advocates, the evaluation based on historical costs has begun to decrease in the last years due to the fact that the American body of normalization FASB and the international one IASB have promoted more and more the concept of fair value. It is the case of the adoption of the model of reevaluation in the subsequent evaluation of the corporal lock-up, the presentation of the financial instruments at fair value in the financial reports, the alternation in the adoption of the evaluation methods, the evaluation of the real estate investments at fair value and the examples can

continue. Plus, in the specialty literature we can find reference at the concept of full fair value.

When judging the virtues of prudence in the construction of the profit and the maintenance of the capital, the advantages of the usage of the fair value cannot be omitted in the financial information, as:

- the evaluation at fair value supplies objective information that takes into consideration the tendencies of the market and the methods of evaluation for the foreseeable flows of treasury;
- a better reflection of the economic reality because the fair value is by the case a **market value** or an **use value**;
- the diminution of the possibilities that the managers have to adjust the desired profit due to the fact that the evaluation is based on exogenous values (as it was mentioned previously: the market value or the use value)

And still, the presence of the aggressive and of the conservation, of prudence and non-prudence in the evaluation of the result in the conditions in which prudence is no longer an obligatory virtue of the accountant evaluation, the problem of finding a new criterion is posed regarding the options in the constructions of the result and the maintenance of the capital. In our opinion, such a criterion can be the one of the **treasury result**. Those methods that influence positively the treasury result are chosen, respectively, aggressiveness in the construction of the treasury result. The formula proposed for the evaluation of the treasury result is the one that emerges from the accountant result based on the commitment book-keeping, using the relation:

- *the accountant profit(loss) in the count 121 „Profit and loss” before taxation*

+ , - *the adjustments in the non-cash elements (example, liquidations and commissions)*
+ , - *the variation of the necessary in the floating asset (the modifications of the circulating assets and current debts)*
+ , - *cash flows in the investment activity (cash/payment regarding the real estate)*
+ , - *cash flows in the financing activity (increase/decrease of personal capitals and non-current debts)*
- *taxation on paid profit*
= **treasury result**

Today, excepting the information regarding the cash flows, the convention of the book-keeping of commitments is accepted, according to which the transactions and the events are recognized and reported in the financial situations when they appear

and not depending on the period when the cash or the cash equivalents are cashed or paid. And still, two conventions should be accepted by synchronism, the **commitment book-keeping** and the **treasury book-keeping**, the reciprocal passage from one to another being possible when the problem of accountant liberties and concordancies is raised.

Final argument

The analysis presented previously leads us to the formulation of the option criterion in the choice of the evaluation methods of the gains/losses, respectively of the assets/debts, *„is the criterion of maximization the treasury result evaluated by direct method?”* Why the treasury result? Because this reconciles the rapports between accountant-financial in the maximization of the enterprise's performance. Through a compared and system analysis within the options of the accountant politics the methods that maximize the treasury result are chosen. Also, this gives expression to the general equation of book-keeping: **assets + expenses = personal capitals + incomes + debts** by appeal at the treasury flows, flows that have the same nature as the capital investment.

In the treasury result we can find the basis and methods of evaluation both of the assets and debts but also of the incomes and expenses. Such a result gives expression to a reality, that is that at the performance production contribute both the activities that consume resources and that produce result but also the assets and debts belonging to this entity.

- *The activity result (realized incomes – expenses corresponding in historical costs)*

+ , - *the result from the possession of the consumed assets: (the expenses corresponding at fair value-the expenses corresponding in historical costs)*
+ , - *the result from the possession of the non-consumed assets (non-consumed assets at fair value – non-consumed assets in historical costs)*
+ , - *the result from the hold assets/debts of treasury (treasury assets – treasury debts)*
= **financial performance**

To sustain the opinion mentioned above, the idea according to which not only any increase of profit is sufficient for capitalizing the fortune invested in the enterprise's assets must be retained. As the Univ. Professor dr. Ion Stancu shows, in the reference book „Finance”, fourth edition 2007, The Economic Publishing House, **„the maximization of the profit has sense at levels superior to the profitableness limit”**, on the contrary, the fortune invested in economic assets would disinvest.

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