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FIGHTING CORRUPTION GENERATED BY ACCOUNTING. CASE STUDY ROMANIA

Abstract*. In the last decades, corruption has become a global problem affecting each country in a different way. In Romania, corruption has a different structure, there are many small corrupt companies and a few big corrupt companies, but the European regulation has a positive impact on reducing corruption on the national level. Nowadays, corruption has become a part of our society. Accounting techniques are important as an efficient instrument for fighting corruption and new information systems improved the financial reporting. In our opinion, it is important to prevent corruption and identify the best accounting techniques to detect and to reduce the effects of corruption.*

Keywords*: financial crime, corruption, government, fraud, accounting.*

JEL Classification: C61, D72, H11, H26, K14

1. Introduction

In this paper we present some current aspects in corruption by examining the petty corruption and grand corruption, how corruption can be affected by accounting regulations and the development of double accounting and triple accounting. Both large and small corruption are related to "public" and "private" matters and often associated with bad governance in the bureaucratic state. In weak countries with civil war and poor economy, the big corruption is snowballing and many public servants are involved in illegal or criminals activities. Thus, citizens need public authorities' protection (Rose-Ackerman, 2008). In the developed countries, the small corruption is growing very slow and corrupted relations are affecting some sectors of European society, such as: diversion of public funds, favoritism in decisions of government officials, irregular payments and bribes, etc. The recent economic crises and corruption affected Romanian economy (Zaman and Goschin, 2014).

We compared the cases of petty corruption with the cases of grand corruption and the results were very interesting, because the big number of cases of petty corruption could be more dangerous than the reduced number of cases of grand corruption. The relation between petty corruption and grand corruption is very strong and systemic corruption could induce bureaucracy to public sector (Zaman and Ionescu, 2014). We identified corruption in double accounting and triple accounting methods and we analyzed the consequences in the companies' financial reports.

2. Petty Corruption and Grand Corruption. Preventing Advantages Against Corruption Damages

In our opinion, petty corruption is related to small incidents from public administration, but also from the private sector and it is better to prevent than cure the corruption damages. Corruption can induce inequality and could affect national economy (Uslaner, 2008). Petty corruption means numerous cases of corruption of relatively small dimensions, but with and unknown summering up results. Grand corruption is related to central administration. In our opinion, grand corruption means fewer number of events, but much larger dimension.

If we should sum up to total number of petty corruption cases, their magnitude could be in one of the following three variants, that are considered in value terms:

1. The first variant where petty corruption could be bigger than grand corruption and priority number one should be the petty corruption:

$$\sum_{i=1}^{n} PC_i > \sum_{i=1}^{m} GC_i ,$$

where:

- m # n and
- n = cases of petty corruption
- m = cases of grand corruption

In this case, there are at least two inherent dangers, as for example the speed of mass diffusion of the negative propagated effects, which could turn into a bigger corruption or grand corruption, and the second danger is the weaknesses of law enforcement which creates the feeling of law violated behavior (law not respected the law).

2. The second variant, where petty corruption is almost equal with grand corruption:

$$\sum_{i=1}^{n} PC_i = \sum_{i=1}^{m} GC_i ,$$

where:

- m # n and
- n = cases of petty corruption
- m = cases of grand corruption

In this case, the attention and concern as regards corruption fighting priorities should be equally distributed in the direction of both petty corruption and grand corruption.

3. The third variant where petty corruption is smaller than grand corruption and priority number one should be the grand corruption:

$$\sum_{i=1}^{n} PC_i < \sum_{i=1}^{m} GC_i ,$$

where:

- m # n and
- n = cases of petty corruption
- m = cases of grand corruption

In this case, usually considered the most frequent one, grand corruption is more important, but the reality shows us that it should be a mistake to consider it as a rule. Anyway, the large part of the special literature and practitioners consider this situation the most critical and urgent as far as fighting corruption priorities are concerned. Some specialists distinguish three categories of corruption, such as:

- petty corruption;
- medium corruption;
- grand corruption.

Of course, we can invent a lot of principles and criteria of corruption classification depending on the aimed objectives. All these above mentioned variants could be observed in real economy with an intensity and frequency depending on:

- economic and social development level of the county, regime or area;
- characteristics of rural and urban regions and populations;
- peculiarities of different economic sectors located in different area or regions.

For instance, corruption in financial sector could be consider bigger or more frequent than in other sectors because of the larger number of ways to transform the big business to small transactions and other ways of hidden accounting. In our research, we identified some priorities in order to prevent corruption:

A. Preventing corruption using financial surveying, such as accounting, controlling and monitoring of economic transactions.

Accounting became like a common global language for business, so that company accounts are understandable and useful for the general public, investors and state (Willow and Keefer, 2015; Cesaroni et al., 2015; Williams, 2014; Ryu and Duvanova, 2014; Prowle and Harradine, 2015; Mulligan, 2015). The role of accounting is to prevent corruption by recording, processing and communication of financial information for managers in order to adopt the best business decisions.

Controlling is a better way to prevent petty corruption by using controlling methods and techniques, such as (Roehl-Anderson and Bragg, 2000):

- ✓ primary operations control;
- ✓ administrative control;
- ✓ accounting control.

Primary operations controls include all the departments and concerns the internal policies and documents of the company. Administrative control represents the monitoring of the internal reports, programs and quality control. Accounting control is the most important one and consists in controlling all the assets and the financial records in order to identify the erroneous recording or fraud.

B. Repairing corruption damages could be done using internal auditing and external auditing.

Internal auditing is based on the results on internal control and usually the controller can suggest a number of internal audits for some suspicious transactions, such as newly signed contracts with no penalty clauses or payroll reports where managers received big bonuses when the company has not recorded profits for two or more consecutive years.

External audit is useful to repair the corruption damages because it is performed by an independent person, who presents the audit report in accordance with the European regulation and national legislation. The investors, government agencies, and the general public rely on the external auditor to present an independent audit report.

3. Accounting and Corruption

There are many ways to register the economic transactions, and the accounting methods have become very complex in the last decades. In order to hide the profits from fiscal authorities, corrupt managers invented different ways to record business transactions:

- real accounting;
- double accounting;
- triple accounting.

The real accounting consists in the normal accounting method where all economic transactions are recorded according to the national and European regulations, all the financial reports are prepared, all the taxes are paid to the state and all the investors received theirs dividends. **The double accounting** consists in a double set of books, one set for the fiscal authorities where the profits are reduced and the assets are under evaluated, in this way the taxes paid to the state are very low. Sometimes, the assets are not properly evaluated and not in time.

The triple accounting case is more complicated because this set of reports presents false profits or false amounts to banks or other investors interested to invest in that company. We think that triple accounting is more detrimental because it misleads to a greater extent a lot of beneficiaries and users of its accounting information. International Financial Reporting Standards (IFRS) could prevent corruption because it gives more means standards and criteria of a more accurate financial figure compilation and reporting. IFRS offers opportunity of a better decision making for general public, economic agents and banking system.

Corrupted behavior could be determined by recording a loss for five consecutive years in Romania, with the possibility of deduction from the current profit for big companies. In many occasions, the example that we present is significant for the profit and loss behavior (Table 1):

Table 1. The profit and loss behavior for the companies

Year 1	- 3.000	Loss
Year 2	+1.500	Profit (deducting loss from the year 1)
Year 3	- 1.500	Loss
Year 4	+ 3.000	Profit (deducting loss from the year 3)
Year 5	- 2.500	Loss
Year 6	+1.000	Profit (deducting loss from the year 5)
Year 7	- 2.500	Loss
Year 8	+2.500	Profit (deducting loss from the year 7)
Year 9	- 2.500	Loss
Year 10	+3.500	Profit (deducting loss from the year 9)
TOTAL loss	**-500**	

Source: Authors' own calculations

The case of triple accounting proves the corrupt behavior of managers in Romania, wishing to pay less taxes to the state, but to keep as much as possible from their profits and to mislead the bank officers and other credit institutions, using the accountant's involvement in preparing attractive financial statements for financial institutions (Table 2):

Table 2. The double and triple accounting for the companies

Real accounting	Double accounting	Triple accounting
For the owners	For the state	For the banks, leasing and insurance companies
Real assets	Undervaluation of assets	Overvaluation of assets
Real profit	Reduced profit	Artificial profit
Real cash and inventories	Little cash and inventories	Artificial cash and inventories
Real work force	Unemployed staff	More employees for short time
Real tax calculated	Less taxes	One time profit tax
Strategic management	**Poor management**	**Good management**

Source: Authors' own work

We could identify comparative advantages among different versions or variants in the sense of costs/benefits analyses and early warning or avoiding and combating the petty corruption and grand corruption. In the case of double accounting the relationship between benefits and costs of this method implementation are the following:

- As advantage, we consider the possibility of revealing the hidden part of profit and the real value of the assets with the intention of tax evasion;

- The costs of this method are related to the dimension of effort deployed by the control entities in order to discover the misused and misunderstood of rules of legal procedures.

This method could be conceived in a double manner:

- on the one hand is the scope of avoiding the violation of rules and procedures in an early stage, what is beneficial for both delinquent and fiscal authorities which are able to receive correct amount of revenues from contributors;

- On the other hand is to collect the amount for taxes from companies according to the total amount of revenues and the accurate value of the assets.

According to our experience and practice the majority **of double accounting cases** are discovered in this early stage due to an effective cooperation, on the one hand, usually between central and local public authorities, controllers and auditors, and on the other hand, due to an efficient involvement of all state holders, such as: National Integrity Agency (ANI), National Anticorruption Directorate (DNA), National Agency for Fiscal Administration (ANAF), Police, Customs, National Office for Prevention and Control of Money Laundering (ONPCSB) and some other foreign control organism at European and International level. The National Agency for Fiscal Administration (ANAF) has become an important agency to fight against corruption and fraud in order to collect taxes, contributions and other social charges (Ionescu, 2015).

As far as **triple accounting** method, we consider as an advantage the possibility to make transparent the artificial devices used by managers to present in an excessive way the favorable financial situation of the company, when they are presenting the necessary documents to the banks, in order to obtain some loans or some capital from other investors, who could be attracted by the falls "rosy figures" of the company: "Everything is rosy in our garden!".

Fighting against the triple accounting is a measure that will contribute to the resetting of the false financial image of the company and restore the real financial truth. Or, undoubtedly, this is a good reason for avoiding eventually undesirable disasters events for both companies and banks and other potential investors. We need to adopt anti-corruption methods in order to protect the business in the global market place (Olsen, 2010).

A very common way to manipulate the property tax in Romania is to evaluate the assets at the end of fiscal year. According to the fiscal code, all the assets are subject to evaluation at the end of December in order to make corrections in accounting books and fiscal evidence for taxation. Usually, provision should be made for assurance that all the assets are properly evaluated in accordance with the accounting principles. For example, a company could evaluate every year one building according to market fluctuation and with appraisal's involvement (Table 3):

Table 3. The evaluation of the buildings

Book value	Double accounting	Triple accounting
1.000.000 lei / year 1	750.000 lei	1.500.000 lei
1.500.000 lei / year 2	900.000 lei	2.000.000 lei
700.000 lei / year 3	600.000 lei	950.000 lei
Value of purchase	Undervaluation because of economic crises	Overvaluation due to modernization and other improvements

Source: Authors' own work

In the double accounting method, the reduced value of the building determines a reduced property tax to the local municipality and a little cost of property for the company. On the other hand, in the triple accounting method the big value of the building determines a favorable and healthy image of the company for the banks or potential investors to put money into. It is the case of some companies to increase theirs assets in order to attract investors or to be financed by banks for Real Estate projects or mergers. Also, a big value of the building could encourage an investor to buy a property for an unrealistic price.

In the financial reports at the end of the fiscal year, the different values of the assets could change the profitability of the company, as presented in Table 4:

Table 4. The Balance sheet of a company

Indicators	Real accounting (company)	Double accounting (fiscal authorities, police)	Triple accounting (banks, insurer, leasing companies)
A. **Fixed Assets**	159.176	159.176	359.176
B. **Current assets**	344.544	332.544	132.544
- Debtors	344.452	332.452	32.452
- Cash and bank accounts	92	92	100.092
C. **Expenses in advance**			
D. **LIABILITIES: amounts to be paid in a period of up to one year**	12.000		
E. **Current assets, net current liabilities**	332.544	332.544	132.544
F. Total current assets minus current liabilities	**491.720**	**491.720**	**491.720**
H. **Provisions**			
I. **Income in advance**			
J. **Capital and reserves**			
I. **capital**	1.000	1.000	1.000
II. **Home equity**			
III. **Revaluation reserve**			
IV. **Legal reserves**	300.969	300.969	300.969
V. **Profit or loss brought forward**	189.000	189.751	80.000
VI. **FINANCIAL YEAR RESULT**	751		109.751
TOTAL OWNED EQUITY	**491.720**	**491.720**	**491.720**

Source: Authors' own calculations

We observe in table no. 4 how the balance sheet could be modified by using the fixed assets and cash in hand and bank accounts, for a certain moment when the indicators are favorable for the company. In the balance sheet the fixed assets are the same for real accounting and double accounting in amount of 159.176 lei, but in the triple accounting fixed assets are over evaluated 359.176 lei, in order to promote the appearance of a healthy image of the company for the investor's eyes. Also, in the triple accounting report the total amount of the cash is 100.092 lei, in order to show a lot of cash-flow to the potential investors.

Accounting could be a cause of the economic crises, but also could prevent financial disasters if the accounting information is accurate. In our research we identified the anti-crises triggers, such as: role of accounting as early warning signal, reducing risk management by implementing accounting procedures and promoting new business by using accurate information from the financial statements and other reports. If we have real and accurate information, we could adopt the best decisions for the company and for future development in order to promote good business and good governance (Nica, 2015; Olds, 2015; Ashford, 2015).

4. Method of Profit Hiding

The profit indicator is one of the most important domain where the corruption could be analyzed taking into consideration the multitude of interests to which each of the numerous stakeholders are involved in. The profit is an interesting result of economic activity which generates an interest overlapping, as follows:

- one the one hand, the corrupt managers try to hide the profit size and the revenues in order to pay less taxes, especially if the feed-back effect of taxes from the state is not sensitive or is not felt to a satisfactory level by the contributors;

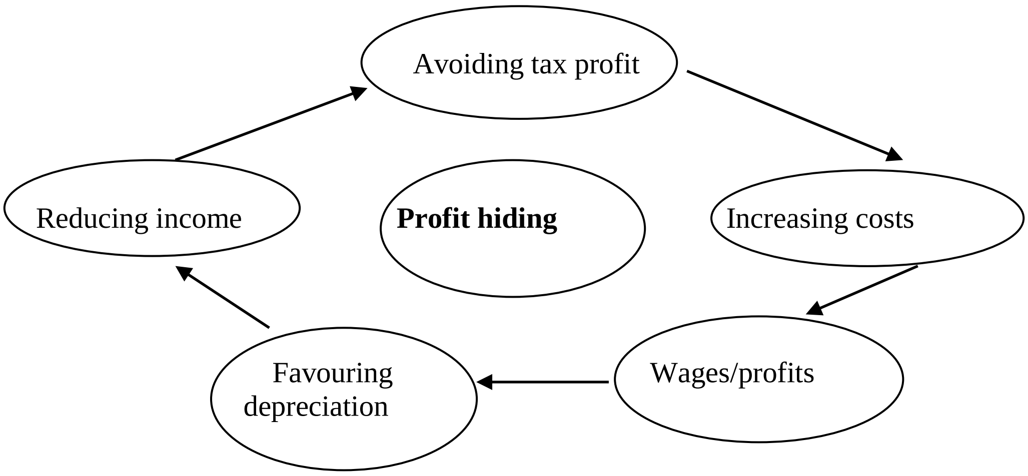
- one the other hand, one could say that there is a whole plethora of specialists trying to identify which are the most adequate techniques and ways for increasing the list of expenditures and costs by inventing all kinds of fees, consulting expenses, per diem amounts for fantasists and touristic or professional visits, or market research and enquiring.

The other way of hiding profits consists in returning profit to tax-haven. Thus, corrupted managers are attracted to these areas with reduce or very law level of taxation relative to their national fiscal system. In the last decades, we could observe a competition between tax-haven areas to attract investors. To a certain degree, this profit hiding behavior of companies is justified especially in the case of corrupted public administration with corrupted public servants because managers think that they do not receive the expected positive effect from their tax payments. All in all, the economic theory and not only, is trying to find an optimal solution for the both ways of corruption behavior (for the corrupted managers and for corrupted public servants).

In our opinion, there are some factors for profit hiding:

- ✓ avoiding tax of profits;
- ✓ reducing the income;
- ✓ increasing the operational costs;
- ✓ favouring depreciation recovery detrimental to real profit for shareholders benefits;
- ✓ wages and profit determinants because the managers and shareholders are interested in obtaining maximum profit, but employees have the desire of wages maximization (Figure no. 1).

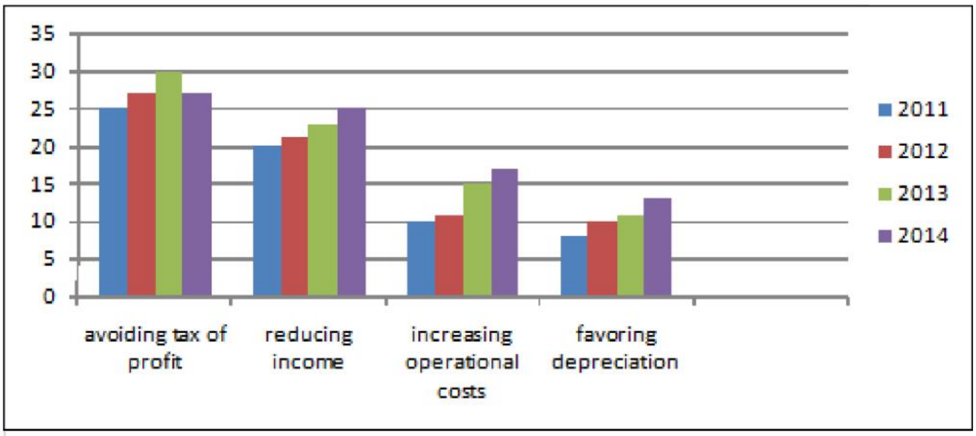
Figure 1: Factors for profit hiding



Source: Authors' own work

Our study sheds some light on the mixed findings and often conflicting results on the important factors for profit hiding. This study was based on survey data collected from more than 200 managers and employees of large and small business organizations. Thus, analysis was conducted using a random sample consisting of 200 respondents from the companies and the survey was finished by the end of 2015. About 57% of respondents were male and 43% were female. About 50% of the participants held various managerial positions (from supervisory levels to senior management) and the majority of respondents had university/ college degrees (75%). Our results generally show a clear relationship between the factors of profit hiding in Romania for the period 2011-2014, such as increasing the operational costs during 2011-2014 in the same time with favoring depreciation in order to reduce the profit and pay less taxes to the state budget (Figure 2).

Figure 2: Survey of data factors for profit hiding period 2011-2014



Source: Data collated by authors

Sometimes, there is a kind of trade off (compromise) between these two groups of actors in order to diminish taxable profit or income and increase especially the operational cost via overcrowding per diem allowances, hotel accommodation costs and travel. Cost pricing exacerbation is a common practice for business. For example, there are some agreements between state and private companies leadership in order to negotiate unfair contracts which permit supply from state to the private beneficiary at lower prices in comparison to the market prices and vice versa. In this way, private firms are selling to the state enterprises at higher level prices which are not in accordance to the market level and the ethic code of business.

For reducing the corruption size, in our opinion, two ways are essential:

- First, the effort to rise the level of conscience of companies managers and investors, in order to determine a so-called "just profit", which should avoid additional components non-justified by the own effects of firm (real costs) and burdening the poverty and discomfort of the beneficiaries;
- Second way consists in implementing a systematic set of measures and sanctions for the cases of corruption found out at the level of public administration. This is closely related to a continued process of improving the public servant behavior and the status of the observers of the law and consolidating the mentality of the "in medio stat virtus,"

in the sense that rapid and non-justified enrichment (actio de in rem verso) sooner or latter occur risk to be discovered.

There are many ways to determine an algorithm (Ruxanda and Smeureanu, 2012), but we propose in this research to find a formula according to which the amount of “just profit” (Jp) had to be determined with the aid of the real profit:

Jp = Rp – N ee, where:
Jp = just profit
Rp = real profit
Nee = non eligible expenses

We consider Jp an affordable profit (Ap) from economic, financial and social point of view and managers are happy to pay the taxes for it. According to this formula, one can figure several scenarios (versions) of corruption evolution, as follows:

V1. Ap = Rp – Nee = 0

In this version, the affordable profit is equal to the real profit and very close to zero because the company is not producing any profit at all.

V2. Nee = constant over time, so Rp will increase, then in time it is expected an increase in affordable profit. In this case, non eligible expenses remain constant for a sufficiently long period of time and the real profit could increase due to the evolution of revenues.

V3. Nee will increase over time, then affordable profit will decrease, which is the worst case. In this case, the real profit is reducing constantly because of the expenses, so the Ap will have the same evolution.

We think that the influence of Nee is very important, because it has become a method of profit hiding and often used by the managers in order to manipulate the Rp and Ap. In order to encourage the companies to declare the real profit and to pay the taxes, the government must to offer more alternatives to reinvest the profits and to develop the national economy.

5. Conclusion

In recent decades, corruption has remained a major cause of poverty and unemployment. Social inequality is a consequence of governments’ policies, accumulating a significant quantity of corrupted behaviors and misguiding priorities, the accountability of which in fact is discovered too late or is not at all discovered. In both cases, the possibility to recover the social prejudice is under the level of real economic loses. Thus, the pyramid of inequality is growing every decade and moving money from the bottom to the top, but those from the top spend less then those on the bottom, this weakening overall demand (Stiglitz, 2015).

Up-to-dately, in spite of institutionally made efforts, the ways of profit hiding, including fiscal havens, seems to exist and survive due to an invisible hand of money power and money laundering. Thus, in order to improve the tax collection and to reduce the number of tentative and intentions of double accounting and triple accounting, we think that a very effective method could be the cooperation between Ministry of Finance and transboundary control authorities with the support of banking systems for those citizens which register arrears and delays in paying their taxes to local and central budgets.

The interdiction to leave the country for bad contributors could be a very good and rapid solution in order to increase the revenues to the state, especially to those business men who set up business in different countries (Popescu Ljungholm, 2015a, b; Koplyay et al., 2014; Leubolt, 2015; Hussain, 2015). This should be rather a method to impose a legal financial discipline than a violation of human rights of movement abroad, as someone could claim against this procedure. Even more, we think that such a measure could be extremely efficient if were be adopted at European or international level. As a matter of fact, our proposal could be without any difficulty included in the frame of verified good practices in the real economy. Of course, the implementation of this measure needs many premises, such as: professional staff in the domain, clear, transparent and rigorous legislation, IT support and political or civil society decided to implement it (de Dijn, 2015; Carr et al., 2015; Muff and Mayenfisch, 2014; Planells-Struse, 2015; Lavinas, 2015).

Fighting corruption generated by double accounting and triple accounting is a necessary instrument for reestablishing the real financial situations of the companies and individuals, and avoiding a lot of financial disasters, which could evolve in a “bule de neige” (snow ball).

Finally, double accounting and triple accounting could be considered one the major causes of the current economic crises because of misleading the decision making process in matter of crediting, financing and good accounting at the level of companies and banks, which are overwhelmed by nonperforming loans. Fighting against double accounting or triple accounting could prevent negative consequences of future economic crises.

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