

Earnings management: the continuum from legitimacy to fraud

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Earnings Management: the Continuum from Legitimacy to Fraud Introduction

Are you going to conduct your fraudulent actions and operations in your business? Maybe it is better for you to make fraudulent actions and to cheat you CEOs? Of course, the answer to these questions should be negative. Nevertheless, in many companies accountants and managers are not afraid of being involved into fraudulent practices. The basic concepts " fraud" and " legitimacy" should be defined. Trochim & Donnelly (2008) develop a reliable basis for concepts considerations and development of further ideas in this research paper. To focus on the basic concepts and to clearly be aware of the essence of the concepts is the first and foremost step in research development. Schram (2006) and Shank (2006) underline that it is very important to identify one concept and separate it clearly from another one. Patton (2002) makes an emphasis on a potential interpretation of key concepts, i. e. we should first identify " fraud" and then pay our attention to " legitimacy". Therefore, we should follow the ideas of bright minds and wise heads of the researchers and believe into their claims that concepts identification is very important in the process of our further research. What is the real meaning of the concept of " fraud"? On the one hand, it is not very easy to identify this concept and very often it is used beyond the context of economy. It is possible to identify the concept of " fraud" in the following way: the way an accountant or a financial manager or any other party involved in the earnings management is involved in the process of cheating, then it is possible to talk about a possible occurrence of fraud (Shelton, Whittington, and Landsittel, 2001). It is very easy to understand and discuss the concept of fraud in relation to earnings management and refer to it as to

cheating the process of gains management of a certain financial entity (Telberg, 2004). It should be mentioned that fraud can occur in case some ephemeral earnings or some hiding of profits or inventing unreal earnings. Hoffman et al (1996) surely claims that the reason for fraud occurrence should be found in subjection of accountants to external pressure. Very often CEOs or stakeholders make the accountants deal with financial management and introduce cheating in their practices. Thus, the company can gain profits in case some unreal financial indicators occur and the earnings management turns into illegal practice. From legitimacy to fraud How to hide real figures of the company's earnings is not a big secret at all. Financial operations are very challenging and it is often difficult to find who is guilty in the wrong doings. Moreover, it should be noted that negative consequences of fraud in earnings management can be dangerous for any company and it can even become a bankrupt. A well-known case of Enron, can illustrate the fact that fraud in accounting led to drastic consequences: the accountants wrote unreal figures in their financial statements and the auditors were cheated. As a result of this action, hundreds of employees lost their jobs and retired employees were left without their pensions (Dooley, 2002). Fictitious transactions are one of the first possible steps on the way to fraud management (Shelton et al, 2001). Ethical aspect of accounting management should never be avoided. It is one of the most crucial issues in the practices of accountants of any company. In case fair practices are avoided, then the companies can suffer losses and be driven into temptation of fraud. Managers and CEOs are often blinded by potential monetary gains and do not think properly about their goodwill, fair market operations etc. To

be flexible in accounting is to be open for cheating and fraud. Nevertheless, Levitt (1998) considered that flexibility can occur in case the company is open for changes and is flexible on the market. Flexible practices in management can result in such drastic consequences as leakage of information, bad data in financial statements and many other possible malpractices. Ethical Concerns Concerning reliability of qualitative research, it can be said that both reliability and validity are two crucial elements in any qualitative order. Patton (2001) underlines that both of these two factors are important for any research. In the process of my research I was collecting the material, analyzing it and implementing in the context of accounting management. Quality of any research can be identified on the basis of the following question: how can my research contribute to other researches and studies in this field. In the paradigm of accounting management there is a wide range of terms, but two main clusters of terms, such as "fraud" and "legitimacy" were identified and correlated terms with these key concepts. Therefore, this research provides a high degree of validity and reliability, because it cedes on the basic terms and concepts of earnings management, is based on theoretical and empirical basis and provides a holistic overview of fraud in earnings management. Conclusion Enron case study is a perfect example of the necessity to avoid fraud in earnings management. The accountants were driven into temptation of hiding real figures in the financial statements of the company and Enron lost its money. From ethical perspective, managers of Enron should be more attentive to reputation of the Company and be aware of potential hazards for the Company (Statement on Auditing Standards, 2010). Therefore, and Proactive practices in

accounting, open and ethical operations are a must in accounting (Trussel & Rose, 2009). Professional activities in accounting practices would result in ethical background in the field of management. Concealment and auditing cannot be correlated at all. To do business legally or not - is a very difficult and challenging question. The modern accountants are often intimidated by the managers and CEOs and they are subjected to their external pressure. It is very difficult for a person to make a right choice. That is why, the boundary between legitimacy and fraud in earnings is vague.

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