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Understanding And Explaining The Underpinnings of Creative Accounting in Nigeria: The Cadbury Evidence

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Abstract - *The rapid decline in public and investors' confidence in the management of public quoted companies as a result of reported widespread incidence of 'widow dressing', 'aggressive accounting' or 'creative accounting' has triggered the need to explore the rationale for such practice. Using Cadbury Nig Plc as a case in point, it is posited in this paper that favorable stock prices tend to give the impression of stability and sustained improvement which in turn, propel to embark on creative accounting in the bid to attract and retain the confidence of shareholders. Arguably, these reasons are offset or nullified by the dangers creative accounting can pose to companies and indeed, the economy. The findings and recommendations of this paper have implications for investors, directors, and policy-makers in Nigeria.*

1.0 Introduction

The accounting profession has through the years tried to develop rigorous system of accounting procedures in the world. Nevertheless, there is still a significant gap, between what the investors and creditors expect and what the accounting profession delivers. This 'expectation gap' exists in part because public companies have a great deal of discretion in choosing accounting estimates that impact on their reported financial results (Okolie, 2006).

Under the statement of Accounting Standard (SAS), the amount of discretion that a company has in preparing financial statements is controlled by two fundamental principles of accounting: conservatism and objectivity. However, in reality, these two guiding principles are often stretched to the limit or sometimes ignored.

When conservatism or objectivity is impaired, creative accounting is prospectively promoted. While in theory, a firm's accounting staff should employ procedures that are objective and conservative, in practice, management has many competing motivations. Many companies manipulate accounting figures and embark on deliberate breaches of the accounting system and control in order to facilitate the financial reporting goals established by management. Indeed, many companies misstate their true profitability by creative/aggressive accounting. That is, some companies adopt an extremely aggressive revenue recognitions policy that, while not in technical violation of SAS, has the effect of substantially overstating the company's true profitability. In this regard, virtually all firms use creative accounting tactics to present financial results in a particular light (i.e. the overstating or understanding their true, profitability or financial condition).

1.1 Background of the Study

Creative Accounting and Earnings Quality Management (or often referred to as aggressive or innovative accounting) is a euphemism for accounting method that tends to manipulate or violate the rules of the standard accounting practices.

Creative Accounting is at the root of a number of accounting scandals in the world. For example, **Enron and World Com** in the U.S.A, **Cadbury Nigeria plc, Unilever, African Petroleum** and **Afribank,** in Nigeria. The effect of accounting manipulations can be disastrous, leading to total corporate image and executives at best. Despite the overwhelming concern for such accounting practices, not much systematic study has been undertaken to explore the rationale for the use of creative accounting, at least from the Nigerian context. Accordingly, this study seeks to determine why corporate managers employ creative accounting in the preparation of their financial statements as well as expose the tactics employed by them, so as to enable investors identify companies that significantly misstate their true profitability by this practice.

1.2 Statement of the Problem

In many cases, firm managements wish to show earnings at a certain level or following a certain pattern. As a result, they seek loopholes in financial reporting standards which they can exploit to adjust the numbers as far as is practicable to achieve their desired aim or satisfy their financial projections. These adjustments amount to fraudulent financial reporting when they fall outside the bounds of acceptable accounting practice. This is the main thrust of creative accounting. The principal drivers of such behavior include market expectation, personal realization of a bonus, and status or reputational image within the market or industry. Creative Accounting occurs in the form of financial book padding scandal and outright corruption. These have recently rocked the survival or existence of a number of companies in the world. In the United States (Enron and WorldCom), corporate scandal has resulted in convictions charges against the directors of the firm for their roles in the over-statement of accounts and the deliberate manipulation of the financials. Also, in Nigeria, the scandal in Cadbury Nigeria PLC resulted in the dismissal of its managing director and financial director as well as the suspension of the company's shares on the Stock Exchange Market.

However, the principal motives for adopting creative accounting are not fully specified. Since profit is the major index for measuring corporate performance, it is not fully known if creative accounting has an effect on corporate profitability, hence, stimulating the adoption of the practice.
Against this background, this paper seeks to explore the following issues:

i. The continuous misstatement of true profit by some companies.
ii. The disregard for the principles of conservatism and objectivity in respect to revenue recognition, necessitating the adoption of aggressive revenue recognition policy in the name of creative accounting.
iii. The perceived ignorance of creative accounting amongst investors.

1.3 Objective of the Study

The broad objective of this paper is to determine the effect (or the nature of relationship, if any) of creative accounting on corporate profitability and stock price. If there is a relationship, does this explain why financial managers adopt it? Specifically, the paper seeks to:

i. determine creative accounting techniques;
ii. identify the motives for creative accounting;
iii. determine if investors and shareholders are aware of creative accounting methods;
iv. determine the nature of relationship, if any, that exists between creative accounting and corporate profitability;
v. determine the nature of relationship, if any, between creative accounting and stock price; and.
vi. suggest ways in which financial managers, shareholders, investors and other relevant stakeholders may benefit from the findings of this study.

1.4 Theoretical Framework

1.4.1 Creative Accounting: Background and Overview

It is in increasingly obvious that the public views financial reporting as an elaborate strategy in which only those who know the rules can play. The issue of manipulation of financial information is assuming an increasing proportion in the public eye, and the accounting profession needs to address the issue, both for its own sake and that of its public image. Because this has not been given the attention it deserves, there have been reported cases of corporate abuse and manipulation of accounting numbers. Corruption is so rife in Nigeria that many foreign companies find it difficult to appoint Nigerian to run their Nigerian offices. The average Nigerian executive considers the funds of his or her company as just another window for opportunistic productivity. This generalization is unscientific. You may wish to recast!!.

Thus, the financial press is awash with reports from the financial press on how the management of some corporations have played fast and lose with accounting rules to hype their reported earnings, smooth profit, massage earnings, manipulate earnings per share and to window dress the balance sheet. These manipulations have severe consequences on company. In addition, financial managers always believe that such manipulations mislead the capital market. Examples of companies that have been affected by such manipulations are Cadbury (Nig). Plc, Unilever, African Petroleum and Afribank Nig. Plc. In Nigeria, corporate ethics has gone to the dogs, a number of CEOs have set highly ambitious growth target, which, to achieve this, has resulted in several system abuses - overstatement and deliberate breaches of accounting systems and controls. The average Nigerian companies and banks are run like this (Okolie, 2006).

Corporate governance and responsibility has been sacrificed at the altar of nepotism and corruption. Most companies in Nigeria today are padded up and their financial statement heavily suspicious. At the international level, Enron Corporation, the seventh largest company in the world has made everyone from politicians to comedians aware of the potentially disastrous results of Creative Accounting (Mulford and Comisky, 2002).

Agreeably, we know that companies have a lot to lose when managers play the creative accounting game such as a good reputation and investors' confidence. We may not understand what managers have to gain in exchange for this risk. The gain includes a favourable effect on share price, lower corporate borrowing costs due to an improved credit rating, incentive compensation plans for corporate officers and key employees, and political gains. Indeed, creative accounting is here with us.

1.4.2 Definition of Creative Accounting

According to David Ehrenstein cited in Wikipedia (2007), the term Creative Accounting was first used in 1968 in the United States in the film "The Producers" by Mel Brooks.

In reviewed literature, Creative Accounting has been called different names such as: Earning management

* Earning Quality management
* Innovative Accounting
* Aggressive Accounting
* Earning Smoothing
* Income Smoothing Earnings Management
* Financial Engineering, and
* Cosmetic Accounting.

The preferred term in the USA, and consequently in most of the literature on the subjects is "Earnings Management", but in Europe, the preferred term is "Creative Accounting" and so, this is the term that will be used in this paper. Just as creative accounting enjoys several names, it has several definitions. According to Pietersz (2007), Creative Accounting is defined as "the manipulation of financial numbers, usually within the letter of the law and accounting standards, but very much against their spirits and certainly not providing the "true and fair view" of a company that accounts are supposed to. He further sustained that the typical aim of Creative Accounting is to inflate figures. While trying to explain what Creative Accounting is, he distinguished between "Window dressing" and Creative Accounting. He argued that the term "window dressing" has similar meaning when applied to accounts, but in a broader term that can be applied to other areas. He sustained that in most cases, it is often used to describe the manipulation of investment portfolio performance numbers.

Blake and Dowds (2007), gave the simplest definition of Creative Accounting. They defined it as "a process whereby accountants use their knowledge of accounting rules to manipulate the figures reported in the accounts of a business". Wikipedia (2007), posited that "Creative Accounting and Earnings management are euphemisms referring to accounting practices but certainly deviate from the spirit of those rules." To Wikipedia (2007), Creative Accounting is characterized by excessive complications and the use of novel ways of characterizing income and assets of corporations".

Similarly, Healy and Wahlen (1999) cited by Wikipedia (2007), argued that creative accounting occurs when managers use judgment in financial reporting and in structuring transactions to alter financial reports to either mislead some stakeholders about the underlying economic performance of a company or to influence contractual outcomes that depend on reported accounting numbers. Healy and Wahlen explained that Creative Accounting usually involves the artificial increase (or decrease) of revenues, profits, or earnings per share figures through aggressive accounting tactics. Aggressive / Creative accounting is a form of fraud and differs from reporting error. Meacham and Rockness (1994) cited in Alao (2007), defined Creative Accounting as any action on the part of management which affects reported income and which provides false economic advantage to the organization and may in the long term be detrimental.

Nasar (1993), defined Creative accounting "as the transformation of financial accounting figures from what they actually are to what preparers desire by taking advantage of the existing rules and / or ignoring some or all of them". Griffiths (1986), writing from the perspective of a business journalist observes:

> *"…every company in the country is fiddling its profits. Every set of published accounts is based on books, which have been gently cooked or completely roasted. The figures, which are fed twice a year to the investing public, have all been changed, in order to protect the guilty. It is the biggest contract since the Trojan horse…. Infact, this deception is all in perfectly good taste. It is totally legitimate. It is Creative accounting."*

Jameson (1988), cited in Alao (2007), while explaining what Creative accounting is, argued that the accounting process consists of dealing with many matters of judgment and of resolving conflicts between competing approaches to the presentation of results of financial events and transaction. He argued that this flexibility provides opportunities for manipulation, deceit and misrepresentation. These activities practiced by the less scrupulous elements of the accounting profession have come to be known as Creative Accounting. Blake and Dowda (2007), in trying to define Creative Accounting state that it "involves the repetitive selection of accounting measurement or reporting rules in a particular pattern, the effect of which is to report a stream of income with a smaller variation from trend than would otherwise have appeared"

1.4.3 Motive / Reasons for Creative Accounting

Creative Accounting is intended to mislead users into accepting the picture that preparers of accounts would prefer to see reported. Thus, studies have shown that Creative accounting does exist and it occurs for various reasons. According to Healy and Wahlen (1999), these reasons include influencing capital market expectations and valuation, to increase management's compensation, to avoid violating contracts written in terms of accounting numbers and to reduce regulatory costs. In shedding light to these reasons for creative accounting, they explained that the use of accounting information by financial analyst and investors to value stocks has created an incentive for managers to manipulate earnings to influence the short-term performance of the stock. The evidence gathered by researchers shows that some firms manage earnings for stock market reasons. The frequency of this occurrence has not yet been determined. Some studies show that compensation and lending contracts give an incentive for firms to manage earnings to increase bonuses, improve job security and mitigate potential violation of debt covenants. Creative Accounting, due to regulatory motivation, is another area where researchers have begun to discover evidence. Studies suggest that regulatory considerations can induce firms to manage earnings. There is very little evidence, though, on the frequency of this behaviour and the effect on regulators or investors (see Healy and Wahlen, 1999).

Jones (1992) in Pietesz (2007) state that the motives for creative accounting is to: hide a particularly bad year for the company, to force an exceptionally good year or continue the pressure to always be the best, smooth-out results to give impression of stability or sustained improvement, hide large profit by monopolies under anti-trust threat, and to boost assets to avoid take over.

Mulford and Comiskey (2002) states that the reasons for creative accounting is to have a favourable effect on share price, lower corporate borrowing costs due to an improved credit rating, incentive compensation plans for corporate officers and key employees, and for political gains.

According to Naser and Pendlebury (1992), the reasons for creative accounting are:

i. **For Weakness of current accounting concepts:** For example, the concepts of money measurement, prudence and realization will often lead to omission from accounts. Similarly, the use of historic cost accounting in times of inflation means that the historic cost figures are far below their current values and this adversely affects the gearing ratios. In this situation, a company may use creative accounting to fill the gap between current and historic values.
ii. **To meet expectations of financial statement users:** It was argued by Naser and Pendlebury (1992) that managers are forced by the users of financial information to manipulate their results. Managers justify the use of creative accounting on the grounds that financial analyst and other commentators have a fixation about a few key ratios and numbers in the accounts. The analysts likes to see steady progress in a company's net income, earnings per share etc,

and they react negatively if a company's results are different from the market expectations.

iii. **To hide deterioration in financial performance:** Alternatively, creative accounting might be used to hide deterioration in the financial performance of a company that has been brought about by poor management.

iv. **To satisfy investors' expectation on dividend stability:** There is also an argument that investors place positive utility on dividend stability and pay a premium to the company that offer it. If dividend stability enhances the value of a company's shares, then there is advantage in allowing managers to smooth income and the related dividend through the use of creative accounting.

Blake et al (1995) maintained that discussions of creative accounting have focused on the impact on decision of investors in the stock market. To them, the major reasons for the directors of listed companies to seek to manipulate the accounts include:

i. **Income smooth:** Companies generally prefer to report a steady trend of dramatic rises and falls. This is achieved by making unnecessarily high provisions for liabilities and against asset values in good year so that these provisions can be reduced, thereby improving reported profit in bad years. Advocates of this approach argue that it is a measure against the "short truism" of judging an investment on the basis of the yields achieved in the immediate following years.

ii. **Income-boosting accounting policy change:** Companies directors may keep an income boosting accounting policy change to distract attention from unwelcome news. At the international level, Blake et al (1995) reports on how a change in accounting method boosted K-mart's quarterly profit by some $160 million, by a happy coincidence distracting attention from the company slipping back from being the largest retailer in the USA to the number two slot.

iii. **To maintain or boost the share price:** this is achieved 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. This helps the company to raise capital from new share & issue, offer their own shares in take over bids, and resist takeover by other companies.

1.4.4 Tactics Employed In Creative Accounting

Companies have different tactics or activities with which they use to manipulate earnings. Despite the efforts of the accounting profession to ensure objectivity and conservatism, it is still relatively easy to manipulate accounting numbers through unethical and fraudulent means. The list presented below according to Okolie (2006) provides a high level of overview of how management can manipulate accounting numbers.

1. **By recording transactions incorrectly:** for example, recording a long term contract as though all revenues were earned up front, in order to improve current periods' sales and profits.
2. **By recording transactions early:** for example, backdating a large sale in order to boost current year profits.
3. **Recording transactions late:** for example, forward-dating a large sale in order to smoothen revenues and profits between adjacent years (income smoothing)
4. **Misstating percentages or amount involved in a transaction:** for example, lowering the estimated percentage of sales returns in order to overstate net sales profits for the period.
5. **Misstating the amount of assets or liabilities:** for example, failing to write down the value of impaired assets (loans that are not collectable, inventory that is out of date, etc) in order to improve both reported profitability and financial condition.
6. **Changing accounting methods or estimates for no substantive reason:** for example, change the company's method for bad debts, solely to reduce the naira amount estimated bad debts and increase reported profits.
7. **Using related party transaction to alter reported profit:** for example, engaging in transaction with an unconsolidated subsidiary at favourable prices to the parent, thereby shifting profits to the parent company.
8. **Recording fictitious transactions or amounts:** although rare and clearly illegal, companies have on occasion, falsified transaction in order to improve the reported profit ability and financial condition.

Earlier studies (see Alao, 2007) have also found that management often focuses on the following four types of creative accounting tactics or activities:

I. Decreasing discretionary research and development (R&D) expense.
ii. Decreasing discretionary advertising expenses.
iii. Timing the sale of fixed assets to report gains.
iv. Overproduction reflection and intention to cut prices or extend more lenient credit terms to boost sales and/or to decrease cost of goods sold (COGS)

Graham et al (2004) as cited in Okolie (2006) reported that a number of CEOs interviewed admitted to a number of activities (which are creative accounting activities), such as:

i. Delaying or cutting the travel budgets, and maintenance expenses.
ii. Postponing/eliminating capital investment (to avoid depreciation charges).
iii. Asset securitizations and managing the funding of pension plans.

According to Healy and Wahlen (1999) cited in Wikipedia (2007), Creative Accounting tactics include:

i. Unsuitable revenue recognition.
ii. Inappropriate accruals and estimates of liabilities.
iii. Excessive provisions and generous reserve accounting.
iv. Intentional minor breaches of financial reporting requirements that aggregate to a material breach.

McHugh (1992), sustained that the tactics of creative accounting include:

i. The classification of exceptional/extraordinary items to suit the occasion.
ii. Writing off foreign currency translation losses through reserves while recognizing foreign income related to

foreign assets in the income statement.
iii. Choosing the right time to revalue assets.
iv. Not consolidating finance leasing subsidiaries.

Mulford and Comiskey (2002) also sustained that creative accounting tactics include:

i. The timing of some transactions: genuine transactions can be timed, so as to give the desired impression in the accounts. For example, suppose a business has an investment at historic costs which can easily be sold for a higher sales price, being the current value. The managers of the business are free to choose in which year they sell the investment and so this increases the profits in the accounts.

ii. The use of artificial transactions: artificial transactions can be used both to manipulate balance sheet amounts and to move profits between accounting periods. This is achieved by entering into two or more related transactions with an obliging third party, normally a bank. For example, supposing an arrangement is made to sell an assets to a bank, then lease that assets back for the rest of its useful life, the sales price under a sale and leaseback, can be pitched above or below the current value of asset, because the difference can be compensated for, by increased or reduced rentals.

1.4.5 Ways In Which Creative Accounting Can Be Curbed

Naser and Pendlebury (1992) proffered some ways in which creative accounting can be curbed. They are as follows:

I. Through specific regulations: creative accounting has attracted much attention from accounting regulators over the years. However, the American experience as shown by the massive number of pronouncements from the financial accounting standards board (FASB), suggests that the only way to eliminate the practice is to issue specific standards for particular creative accounting devices. Similarly, it is believed that one way to eliminate the practice of creative accounting in Nigeria is the Nigerian Accounting Standards Board (NASB) and professional accounting bodies to continue to make pronouncements that border on discouraging creative accounting activities. The role of regulation is simply to ensure that creative accounting is kept within tolerable limits. The argument against this is that more and more detailed rules might simply lead to resourceful managers devising evermore ingenious schemes to get around them (Naser and Pendlebury 2002).

II. Detecting and reporting creative accounting by auditors: another way in curbing creative accounting is by making it the responsibility of auditors to detect and report on instances of creative accounting. Generally, auditors are expected to apply due care in carrying out their audit functions, where this is compromised, the chances of spotting creative accounting becomes slim.

III. Legislative Actions and punishment: the researcher posits that shareholders of affected companies of creative accounting practice should take legal action against perpetrators of creative accounting. It is important, not only to take serious legal actions against this people but also to punish them with appropriate jail terms. This will deter others from it.

In conclusion, Naser and Pendlebury (1992) argue that there is no completely effective to curb creative accounting and it might have to be accepted as a fact of life due to the following reasons:

i. it has a favourable effect on share prices.
ii. It provides lower corporate borrowing costs due to an improved credit rating.
iii. It provides incentive compensation plans for corporate officers and key employees for political gains.
iv. It helps to retain and attract the confidence of shareholders.

1.4.6 Dangers of Creative Accounting

i. The company loses its good reputation and investors' confidence and this will take the company a number of years to recover.
ii. It helps in killing the value of the company's shares in the stock market.
iii. It can lead to a serious threat to the integrity of financial reporting.
iv. It will result in a reluctance to use statutory accounts for decision making.

1.5 Creative Accounting And Corporate Profitability: The Cadbury Case

Corporate profitability is the relative tendency of profit making in alternative courses of action or decision (see Ilaboya 2005 in Okolie, 2006). In taking investment decision, an investor or financial analyst will have to determine which investment (or company) is more profitable. Specifically, the investor will concentrate on the analysis of profitability indices of the company. Although the other ratios (Liquidity ratios and Leverages ratios) can reveal interesting things about the company, the profitability indices are the ones that give the net result of all the activities and decisions of the company (Nzewi, 2004).

Also the profitability ratios enable the analyst to compare companies in one industry to determine the one that appear to be the most profitable. In the main, the ratios reveal how efficiently the company is utilizing the resources available to it in generating profits that will eventually determine the value of the shares. The profitability ratios thus become a measure of financial efficiency or earning efficiency. They are useful not only in showing the level and direction of earnings but also in revealing what will happen to earning if sales or operating assets are increased or decreased (Nzewi, 2004).

Some of the profitability and earnings ratios which the analyst or investor will be interested in may include:

* Earning per share
* Dividend per share
* Return on sales
* Return on investment
* Price earning ratio
* Earnings yield
* Dividends yield
* Dividends cover

At this point, it is important to relate creative accounting with

Corporate profitability. The review of literature in this regard shows that Creative accounting has a direct relationship with profitability. The nature of this relationship is such that most creative accounting activities reflect in an increase in corporate profit (see the case of Enron Corporation as explained by Mulford and Comiskey 2002)

Collaborating the foregoing, the Cadbury case further explained the relationship between creative accounting and corporate profitability. The writer will therefore concentrate on two profitability ratios i.e Earnings per share (EPS) and Dividend per share (DPS) to give a deeper insight on the relationship between Creative Accounting and Corporate profitability. Before this, it is important to briefly explain the concept of earnings per share and dividend per share.

Earning Per Share

According to Nzewi (2004) it is the rate of return that accrues to the shareholders on each share held. It is the most popular index for evaluating an investment in shares, it is obtained by dividing the residual earnings by the number of share outstanding.

$$EPS = \frac{\text{Earning after interest and tax}}{\text{Number of common shares outstanding}}$$

Dividend Per Share

Once dividends are declared, they are distributed pro rata amongst all shares currently ranking for dividend. The dividend accruing to each share held is the dividend per share. It is obtained by dividing of earnings for distribution as dividend by the number of shares currently ranking for dividend.

$$DPS = \frac{\text{Total amount of earnings for distribution}}{\text{Number of shares currently ranking for dividend.}}$$

Using data from Cadbury's annual report as shown in Table 1.1 below, we explain the relationship between creative accounting and corporate profitability.

Table 1.1

CADBURY'S PROFIT AFTER TAX, EARNINGS PER SHARE AND DIVIDENDS PER SHARE FOR THE YEARS 2002-2006

Year	PAT	EPS	DPS
2002	2,249,079	300	150
2003	2,684,927	357	175
2004	2,812,623	281	160
2005	2,710,921	270	130
2006	(4,665,459)	(428)	-

Source: Cadbury annual report and accounts 2002-2006

Table 1.1 above seeks to explain the relationship between Creative Accounting using profitability indices of EPS and DPS. As clearly shown in this table, Cadbury Nig Plc within the period affected by Creative Accounting (2002-2005), the PAT showed a steady increase in profit. Not withstanding the slight drop in 2005. It is evident that the creative accounting activities of Cadbury could be said to be one of the factors responsible for the upward trend in the company profit position. The loss recorded in 2006 is not a surprise because it is in this year that creative accounting practice was discovered in Cadbury Nigeria Plc and efforts were made to correct the accounts which culminated into the loss.

The EPS and DPS of Cadbury Nig. Plc further provide an insight in explaining the relationship between creative accounting and corporate profitability. The EPS and DPS seem to follow the pattern with the profit profile of Cadbury (i.e an upward trend). However, the EPS and DPS of 2004 reveal otherwise. Although there was an increase in profit from 2002-2004, this was not reflected in a similar trend in the EPS and DPS in the same year. This however did not rule out the existence of creative accounting in those years. Other factors such as change in the number of common stock outstanding and number of shares currently ranking for dividend could be responsible for this. The profit of the company maintained a steady increase during the period affected by creative accounting practices.

1.6 Stock Prices And Creative Accounting: The Cadbury Case

One of the main thrust of this study is to determine the impact of creative accounting on stock prices. Since Cadbury Nig Plc is used as the study focus, we present here a table showing the stock prices of Cadbury Nigeria for December 2006, being the period after the news was widespread of fraud and financial statement padding by the managing director and financial director of Cadbury Nigeria Plc.

As depicted in Table 1.2 (on page 31), the stock price of Cadbury Nigeria (see third column was fast dropping). Although the stock prices in the past four days in December was the same, however, the stock price of Cadbury Nigeria continued to show a downward slide, especially at the heat of the reported scandal.

Table 1.2 shows the behaviour of stock prices at a time when creative accounting scandals were rocking the integrity of Cadbury. The implication of this is that where a company embarks on creative accounting, the company dies slowly. When the creative accounting practice is discovered, and the news spread, this affects the integrity of the firm, which in turn adversely affects the stock prices of the firm.

Since Table 1.2 did not show the relationship between stock prices and profit in a period where creative accounting was rife. Table 1.3 addresses this, using figures from financial statement of Cadbury Nig Plc.

Table 1.3

CADBURY STOCK PRICES AND AFTER TAX PROFIT FOR THE YEAR 2002-2006

Year	Stock Prices	Profit after Tax (PAT)
2002	33.20	2,249,079
2003	63.20	2,684,927
2004	60.20	2,812,623
2005	65.52	2,710,912
2006	32.40	4,665,459

Source: Cadbury's Annual Report

Table 1.3 shows Cadbury stock prices at different year and a five year financial summary of their profits. The period covers 2002-2006. this period is considered to be the period when the managing director and financial director were actively padding up the company's financial statements. As shown by the table, the profits of the firm increased from 2002 to 2004 and this also stimulated an increase in the stock prices of the firm for those years. However, the year 2006 figures were different. The company recorded a loss and the stock prices of the company significantly dropped from #65.52 to #32.40. The reason for the loss in 2006 is because the scandal was discovered in that year and the chairman Dr. Uduimo Justus Itsueli has to find ways to tidy the account of the firm. The overall effect of this on Cadbury stock is a downward slide.

1.7 Creative Accounting And Investors' Awareness

The cases of creative accounting are generally carried out with the intention of swaying the shareholders of the company into believing that the financial report represents actual performance of the firm. The import of this is that the shareholders are generally not aware that their financial reports have been creatively prepared; regardless of the fact that the falsified financial statements were audited by an independent auditor who in most cases collaborate with the management staff to present a false financial report.

Eventually shareholders or investors perhaps, due to their lack of accounting skills and non awareness of possible scandals in the financial statement, usually declare dividends on the basis of false financial report. The implication of this is the payment of dividend from the company's capital.

The level of awareness of possible creative accounting in most companies in Nigeria is low. Therefore, it is imperative that the awareness be heightened so that the incident of shareholders losing their investment would be nibbed in the bud. The effort of creating this awareness should be a concerted one involving the academia, the financial regulatory agencies such as Securities and Exchange Commission (SEC) and also the shareholders.

The current position of SEC on Cadbury case is a good example on the awareness created by government. Not only does the decision taken by SEC on the mismanagement staff of Cadbury and its independent auditor serve as a deterrent and warning to firms currently perpetrating this act, but also it serves as an eye opener to all shareholders of companies on the existence and possibility of creative accounting in their firm. This will help them in taking a more conservative posture in scrutinizing and approving the financial statement for the purpose of declaration of dividend.

1.8 Summary

Creative accounting is a process whereby accountants use their knowledge of accounting rules to manipulate figures for presentation. Different appellations, such as earning quality management, innovative accounting, aggressive accounting, have been used to describe the process. The interplay of several factors influences the use of creative accounting. These include the need to: meet the expectations of financial statement users; hide deteriorations in financial performance; satisfy investors' expectation on dividend stability etc. A number of techniques have also been employed to achieve creative accounting; these include recording transactions incorrectly, recording transactions early, misstating the amount of assets or liabilities, and changing the accounting methods. Creative accounting has economic consequences. The danger of creative accounting is that it destroys the value of the company in the stock market; it erodes company's reputation and investors'

TABLE 1.2
DAILY OFFICIAL LIST OF CADBURY STOCK PRICES AS AT DECEMBER 2006

Date	Number of deals	Quotation	Quantity traded	Value of shares	Per
1/12/2006	23	54.15	36,859	1,995,914.85	0.00
4/12/2006	6	54.15	23,404	1,267,326.60	19.3
6/12/2006	26	54.15	46,368	2,510,827.20	18.46
11/12/2006	14	54.15	11,965	6,17,90475	19.30
12/12/2006	8	51.45	45,725	2,376,292.35	18.42
13/12/2006	4	48.88	24,475	2,376,292.35	18.42
14/12/2006	16	46.44	138,479	6,430,964.76	19.3
15/12/2006	13	46.44	10,596	469,8145.52	-
20/12/2006	25	39.63	35.062	1.396,519.46	18.55
21/12/2006	26	37.84	23,642	894,613.28	17.62
22/12/2006	18	35.95	31,940	1,148,243.00	16.74
27/12/2006	8	34.16	20.520	700,963.20	-
28/12/2006	6	32.40	18,528	6001,418.88	14.36
29/12/2006	12	32.40	11,773	363,618.78	14.36

SOURCE: Daily Official list of Nigeria Stock Exchange. The Guardian Newspaper, Dec1-29, 2008.

confidence. The evidence of this study shows;

1. That there is a relationship between creative accounting and corporate profitability.
2. That creative accounting has an effect on stock prices.
3. That investors and shareholders are seldom aware of the existence of creative accounting.
4. That the propensity of creative accounting by directors is high, especially in the context where corporate profit is used in evaluating the performance of the directors.
5. Directors of company employ a number of tactics to manipulate the financial statement of the company. This tactics is known as creative accounting tactics.

The foregoing relationships are facilitated by:

i. recording transaction incorrectly, early or late
ii. misstating percentages or amounts in transactions, or the amounts of assets or liabilities;
iii. switching from one accounting policy to another ;
iv. charging expenses to reserves instead to profit and loss accounts;
v. capitalizating revenue expenses;
vi. overstatement of sales; and
vii. overvaluation of stock

1.9 Recommendations

The following are suggested recommendations:

i. It is recommended that a special training session on detecting creative accounting in financial statement be held before the Annual General Meeting (AGM) of companies. Such training sessions should be at the instances of the shareholders. The trainers are expected to be persons with in-depth knowledge on creative accounting. This training will expose the shareholders to the various tactics employed in creative accounting, and thus will enable them examine the financial statement properly before they give their approval.
ii. Since companies submit their annual account to Federal Inland Revenue Service (FIRS) for the purpose of taxation, the Board should be mandated to further investigate such accounts to determine the extent of compliance with enabling laws and standards. They already have the power.
iii. It is recommended that the Nigeria Accounting Standards Board (NASB) should be empowered to accept, review and investigate financial statements of all companies operating in Nigeria to ensure total compliance with the General Accounting Practices (GAAP), Statement of Accounting Standard (SAS), Company and Allied Matters Act (CAMA), and other financial reporting Acts before publishing accounts of public companies.
iv. It is recommended that regulatory agencies of the financial sector, such as the CBN, NDIC, NAICOM, and the Securities and Exchange Commission (SEC) should increase penalties and sanctions for directors caught in creative accounting activities. This may serve as a deterrent for any director nursing the idea of creative accounting.

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