GAP GYAN
A GLOBAL JOURNAL OF SOCIAL SCIENCES
(ISSN – 2581-5830)
Impact Factor – SJIF – 4.998, IIFS - 4.375
Globally peer-reviewed and open access journal.

"CONTEMPORARY ISSUES IN ACCOUNTING AND FINANCE"

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Abstract

This research work, as its title indicates, considers some of the contemporary issues in accounting. Its key focus is on issues in Accounting and Finance. Accounting can be defined as the regular reporting of the financial position and performance of an entity through financial statements issued to external users. This definition is relatively straightforward but Accounting is neither straightforward nor simple. As this research work shows, the influences on financial accounting are many and complex, and often the application of financial accounting principles and practices in specific contexts brings unique challenges. Accounting is often cited as the 'language of business' and Accounting provides much of the public information about business (and non-business) entities that people rely on to make decisions. If the Accounting information provided is not 'right', this can have significant adverse consequences for not only shareholders but also the public, the managers of businesses and accountants themselves. Even a brief look at well-known business failures (such as Enron, WorldCom, HIH, One. Tel and the global financial crisis) confirms this. Some accounting students may question why there are issues or problems in accounting that are different from those in the past. After all, the basic building blocks of accounting — the debit and credit rules — have not changed for centuries. Perhaps any problems that have occurred, and related accounting failures, are simply due to a misapplication of accounting rules; that is, the 'right' accounting was not followed. Almost all economic entities irrespective of their size, turnover, ownership, goods or services produced or traded have realized the fact that the human resources is their single most valuable and long-lasting resource which is capable of contributing heavily to the revenue or income generating activities. Hence, the corporate undertakings started thinking of accounting assets status to their human resource which it rightly deserves.

INTRODUCTION

One of the unique features and problems of accounting is not the non-availability of solution to problems of accounting but the availability of more than solution to each one of a few major Accounting problems. Inventory valuation; computation of annual depreciation; treatment of good will, overtime premium, idle time, costs, research and development costs are some of the examples for the accounting problems with diverse solutions. What is more important is that all those alternative diverse solutions are reckoned as sound practices by the professional accounting bodies. What is much more important is that the corporate entities are allowed to use any one of those accepted methods. Consequently, the financial results of corporate enterprise lack comparability their performance is influenced by even the diverse accounting methods. Another important problem is, for some of the emerging accounting problems, no objective solution is available. In other words, for some of the contemporary or current accounting issues, single objective accepted solution is available. That means, there are a number of suggested methods as to how to assess the monetary equivalents of certain new kinds of accounting problems. Consequently, the corporate enterprisers have option to use any one of these suggested method, can manipulate their accounting figures and the financial performance to suit their requirements. As a result, users of accounting information, moves particularly the external parties are deprived of objective, comparable and reliable information.

OBJECTIVES

In this background, an attempt is made to identify and discuss the contemporary issues in accounting. Some of the current accounting issues are:

- Accounting for price level changes
- Valuation of accounting for human resources
- Accounting for intangible assets
- Brand accounting
- Environmental accounting
- Accounting for social responsibility of business

- Nation income accounting
- Creative accounting

REVIEW OF LITREATURE

Naser K (1993) studied the creative financial accounting, its nature and uses. Bornea A, Rohen J and Sadan J (1976) examined the classificatory smoothing of income with extraordinary items. OriolAmat, John Blake and Jack Dowds (1998), Copenland R.M (1968) and Merchant K.A and Rockness J (1990) analyzed the ethics of managing earnings and creative accounting.

RESEARCH METHODOLOGY

A systematic search was conducted to understand and analyze some current accounting problems. Many important reports and articles were used for reference.

RESULTS, ANALYSIS, DISCUSSIONS

Some current accounting problems are (1) accounting for price level changes, (2) accounting for human resources, (3) accounting for intangible assets, and (4) brand accounting.

Accounting for price level changes/ Inflation Accounting
Accounting for price level changes In the light of continuous rise in prices, the methods to account for price level changes were developed. These attempts resulted in the development of a few approached to account for price level changes including (a) general or current purchasing power method and (b) current cost accounting method.

Current Purchasing Power (CPP)
Under the CPP method, monetary items and nonmonetary items are separated. The accounting adjustment for monetary items is subject to the recording of a net gain or loss. Nonmonetary items (those that do not carry a fixed value) are updated into figures with an inflation conversion factor equivalent to the consumer price index (CPI) at the end of the period divided by CPI at the date of transaction.

Current Cost Accounting (CCA)
The CCA approach values assets at their fair market value (FMV) rather than historical cost, the price incurred during the purchase of the fixed asset. Under the CCA method, both monetary and nonmonetary items are restated to current values.
In the light of continuous rise in prices, the methods to account for price level changes were developed. These attempts resulted in the development of a few approached to account for price level changes including (a) general or current purchasing power method and (b) current
cost accounting method. Here, the total impact differs from one approach to another because of three important reasons:

1. Common (general) price indices are used under general purchasing power method, whereas specific price indices are used under current cost accounting method.
2. Under general purchasing power method, all the items of financial statements are restated in terms of the price level at the end of the accounting year. And under current cost accounting method, important items are restated in terms of the average price level during the accounting year; and
3. In the use of general purchasing power method, all the items of financial statements are restated, whereas in the case of current cost accounting method, only three major items for groups of items of financial statements are restated. The three major items are (a) cost of sales (b) depreciation and (c) monetary working capital. As a result, the users of accounting information will be deprives of comparable information.

Valuation of an Accounting for human resources / Human resource Accounting Human Resource Accounting is the process of identifying and measuring data about Human Resources and communicating this information to the interested parties. It is an attempt to identify and report the Investments made in Human Resources of an organization that are currently not accounted for in the Conventional Accounting Practices. Thus, Human Resource Accounting is a term applied by the Accountancy Profession to quantify the cost and value of employees of their employing organization. Quite a few Models have been suggested in the past for the Human Resource Accounting and these can be classified into 2 parts each having various Models. Some of the Important ones are:-

A. Cost Based Models

- ❖ Capitalization of Historical Costs Model
- ❖ Replacement Costs Model
- ❖ Opportunity Cost Model

B. Value Based Models

- ❖ Present Value of Future Earnings Model/ Lev and Schwartz Model
- ❖ Reward Valuation Model/ Flamholtz Model
- ❖ Valuation on Group Basis

COST BASED MODELS

I. Capitalisation of Historical Costs

As per this Method of HR Accounting, the sum of all costs related to Human Resources (i.e. Recruitment, Acquisition, Formal Training, Informal Training, Informal Familiarisation, experience and development) is taken together to represent the value of the human resources. The value is amortised annually over the expected length of the service of individual employees and the unamortised cost is shown as Investments in the Human Assets. If an employee leaves the firm (i.e. Human Assets expire) before the expected service life period, then the net value to that extent is charged to the Current Revenue.

II. Replacement Costs

The Historical Cost Method was highly criticized as it only takes into account the Sunk Costs which are irrelevant for Decision Making. Thus, a new model for Human Resource Accounting was conceptualized which took into the account, the costs that would be incurred to replace its existing human resources by an identical one.

❖ Individual Replacement Costs – which refers to the cost that would have to be incurred to replace an individual by a substitute who can provide the same set of services as that of the individual being replaced

❖ Positional Replacement Costs – which refers to the cost of replacing the set of services referred by an incumbent in a defined position

Thus, the Positional Replacement Cost takes into account the position in the organization currently held by the employee and also the future positions expected to be held by him.

III. Opportunity Cost Model

This model was advocated by Hekimian and Jones in the year 1967 and is also known as the Market Value Method. This method of measuring Human Resources under this Model is based on the concept of opportunity cost i.e. the value of an employee in its alternative best use, as a basis of estimating the value of human resources. The opportunity cost value may be established by competitive bidding within the firm, so that in effect, managers bid for any scarce employee. A human asset therefore, will have a value only if it is a scarce resource, that is, when its employment in one division denies it to another division.

I. Present Value of Future Earnings Model

This Model of human resource accounting was developed by Lev and Schwartz in the year 1971 and involves determining the value of human resources as per the present value of estimated future earnings discounted by the rate of return on Investment (Cost of Capital).

II. Reward Valuation Model/ Flamholtz Model

Flamholtz advocated that an Individual's Value to an organization is determined by the services he is expected to render. This model of Human Resource Accounting is an improvement to the "Present Value of Future Earnings Model" as it takes into account the probability that an individual is expected to move through a set of mutually exclusive organizational roles or service states during a time interval. Such movement can be estimated probabilistically by using the following model.

III. Valuation on Group Basis

While applying the above models, the Accountants realized that proper Valuation as per Human Resources Accounting is not possible unless the contributions of the Individuals as a Group are taken into consideration. An Individual's expected service tenure in the organization is difficult to predict but on a group basis it is relatively easier to estimate the percentage of people in a group likely to leave the organization in the future.

Accounting for Intangible Assets

The corporate enterprises are investing and spending increasingly higher amount of money for the acquisition, development maintenance, enhancement of intangible assets such as scientific or technical knowledge; designs and implementation of new processes or systems including brand names and publishing titles; computer software; patents, copyrights, etc. These assets contribute to the future economic benefits in various forms including (a) revenue from the sale of goods and services, (b) cost savings or (c) other benefits resulting from the use of the asset by the organization. That means, these intangible assets possess the ability to contribute to the stream of revenue or income generation. Hence, they are recognized and assets by the corporate enterprises. Further, the accounting standard prohibits the reinstatement of expenditure recognized as an expense in previous annual financial statements or interim financial reports. 1 Only subsequent costs (i.e., the costs incurred after the time when the Intangible Assets first metes the recognition criteria) which amount for substantially and comparatively lower share in the total cost of intangible assets are capitalized and amortized

Brand Accounting

Brand has been defined as a distinguishing symbol mark, logo, name, word, sentence, or a combination of these items that companies use to distinguish their product from others in the market. Brand has created positive sentiment among the target audience, the firm is said to have built brand equity. Further, applying a trade name to a product or service is called branding and the legally protected brand names are called trademarks. A brand is a type of intangible assets. 2 There are a number of ways to assets the value of a brand. These include: cost based approaches (historical cost method 3 and replacement cost method), market-based approaches (comparable market value method 4 and comparable royalty rate method 5), economic approaches (capitalization of earnings method and royalty) and other approaches.

Creative Accounting

The financial reports which comprise of, amongst others, the financial statements (viz., profit and loss account, and balance sheet) are expected to possess the valuable information content. These reports should contain valuable, relevant, accurate and objective facts and figures.

Meaning of creative accounting

The terminologies like earning management, earnings smoothing, financing engineering, income smoothing, cosmetic accounting, disclosure management, innovative accounting, etc are used to donate creative accounting. A few definitions presented below bring out a few dimensions of creative accounting.

The reasons as to why the Companies or managements resort to Creative Accounting vary from one company to another and also from one year to another. The important reasons are:

1. Income-based Tax System for using Creative Accounting so that the taxable income can be manipulated, at least in the short-term, which will minimize the company's tax burden.

2. Income Smoothing: The corporate enterprises normally prefer to report a study and consistent growth in profit (even if it is at lower rate) than reporting volatile profits which vary from one period to another substantially.

3. Big Bath Accounting (e.g., in the case of recently Taken-over Company): when a company realizes, that, it is going to incur loss for the current year and when the company also realizes that there is no way to avoid loss-incurring situation

4. Matching Report Profit to Profit Forecast: The companies prefer to report, more or less, the same amounts of profit as forecasted prior to the commencement of the accounting period.

5. Matching Actual Profit with Analysts' Expectations or Predictions especially when the company intends to have longer capital market transactions.

6. Profit-based managerial Remuneration is another strong motive for manipulation of profit figures by the managerial personnel.

7. Insider trading is one of the important reasons for distorting the financial results (when managerial personnel engage in insider trading).

8. To Maintain or Boos the Share Price is another reason to manage earnings at the desired level.

9. To Distract the Stakeholders Attention from Creative accounting to report higher profit than the actual profit.

10. When a Company's borrowing capacity is linked to its Capital and Reserves, and are nearing the maximum limit, the company may resort to manage its earnings which in turn improve its reserves, and therefore, its borrowing capacity.

11. Price Revision Policy Pursued by the Governments with respect to their public utilities is another motive for the public utilities to report less profit and obtain permission from their Government-owners to increase price.

CONCLUSION

Numbers are traditionally the accountant's domain. Businesses trust that professional accountants and auditors will maintain, monitor and deliver the required figures to report their activities. But increasingly a mastery of numbers is not the only task expected of the modern accountant or finance professional. Business decision makers need to have confidence in the data that they use to make decisions, but they also need to understand what is behind the headline figures. They need to follow the trends to anticipate new business markets and opportunities, to be aware and mindful of the environment in which they operate and have confidence in the ability of their accountants to step up and contribute to a range of contemporary issues.

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