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   STATEMENT OF THE PROBLEM

   OBJECTIVES

   HYPOTHESES

   RESEARCH METHODOLOGY

   RESULTS & DISCUSSION

   FINDINGS

   RECOMMENDATIONS/SUGGESTIONS

   CONCLUSIONS

   SCOPE FOR FURTHER RESEARCH

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CONTRIBUTIONS TO BOOKS
- Sharma T., Kwatra, G. (2008) Effectiveness of Social Advertising: A Study of Selected Campaigns, Corporate Social Responsibility, Edited by David Crowther & Nicholas Capaldi, Ashgate Research Companion to Corporate Social Responsibility, Chapter 15, pp 287-303.

JOURNAL AND OTHER ARTICLES
- Schemenner, R.W., Huber, J.C. and Cook, R.L. (1987), "Geographic Differences and the Location of New Manufacturing Facilities," Journal of Urban Economics, Vol. 21, No. 1, pp. 83-104.

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- Garg, Sambhav (2011): "Business Ethics" Paper presented at the Annual International Conference for the All India Management Association, New Delhi, India, 19–22 June.

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- Kumar S. (2011): "Customer Value: A Comparative Study of Rural and Urban Customers," Thesis, KurukshetraUniversity, Kurukshetra.

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EARNING MANAGEMENT – OPPORTUNITY OR A CHALLENGE

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ABSTRACT

Earning management is art of managing the books in creative way. It sometime creates wrong impression about the company in the mind of stakeholders and facilitates the management to fulfill personal objectives. In recent earning management cases it has been observed that the real players of numbers are top level managers and directors who are doing it as regular course of their business. In growing and developing economy like India it is very important to understand how such practices may affect the corporate world and economy in long run. India has been considered as most attractive market for investment these days and over this if cases like, Citi bank, Satyam Computers and 2 G Spectrum takes place, potential growth of economy may get affected. The present paper aim to identify the reason of earning management and various facilities companies get from regulatory system to fulfill personal objective. The ethics of motivation to indulge in earning management practices will also be discussed to ensure the legality or illegality of such actions. Lastly, the paper aim to draw attention of regulatory bodies towards the probable threat and challenge which may create problems in growth and development of Indian corporate.

KEYWORDS
Creative accounting, Earning management, Ethics and corporate governance, Regulatory bodies.

INTRODUCTION
Earning management is an art of manipulating books to accomplish the predetermined targets. Although many times such practices are not considered as fraud or unethical unless intentions are cleared. Making the best use of alternatives or choices available in accounting system is ethical and duly allowed by system but when methods are selected to manipulate the books or for creating fake image of company's performance in the mind of investors then such practices are considered as unethical and immoral. Earning management is the transformation of accounting figures from what they actually are to what perpetrators desire by taking advantage of the existing rules and/or ignoring some or all of them.

In India the concept of earning management is new for stakeholders but in many developed countries like UK and Europe the concept is very much popular. It is also known by cooked books, income smoothing and creative accounting. India being an attractive market is required to concentrate on corporate actions and practices in order to create an ethical corporate image in international market. And to support that many steps have already been taken and many are in pipeline.

India is one of the countries which turnaround after global financial crises and is becoming one of the most attractive investment choices for investors all over world. Recent decision of Wall mart and Starbucks to come in India shows how much global players are interested in testing their luck in India. Many more major players are looking India as most attractive market that forces India to think over maintaining the brand image of country. The path to reach at that stage is not easy for India as there are many problems and challenges, acting as roadblock for the economy. Growth in financial and commodity market, micro finance, mergers and acquisitions and foreign exchange market, attracting many unexpected investors. But on the same side this growth is affected by many problems which may spoil the image and goodwill of Indian corporate sector.

Today there are numbers of such services available which finance newly established firms or entrepreneurs having profitable ideas and such services have proven successful also. But the functioning and practices of these services are not known properly to either market or companies which are financed. Similarly, many mergers and acquisitions are taking place by Indian companies, which shows the growth and capability of Indian corporate, but the purpose or objective of such actions are not defined to stakeholders. Lastly, investors always prefer to invest in most profitable firms but do not understand or segregate real profitable companies or nominal profitable companies. These are some most ignored areas in today's competitive environment that may create threat and challenges for Indian corporate to fulfill the expectation of international market.

What is required from Indian corporate these days is trust and faith, by investors or market because even after many norms or regulations and their implementation, investors are helpless to get insight of functioning of companies and they have to rely on information provided by management. Regulatory bodies have given many protective norms to protect the interest of investors but failure on part of companies to implement same is leading to problems of trust among prospective investors. Today investors are very active and want to think and analyze the system before investment decision; they are ready to spend money on advisors or consultancy. But sometime relying on advisors or expert's advice also create problems in wrong investment decision due to two important reasons; first when expert is not expert enough in concerned areas, second, when advice is based on personal gains or objectives. And in many economies latter failure on part of advisors are more prevailing which duly facilitate the management to manage the earnings in desired manner. Thus there is a need of system where safety and trust can be ensured.

RESEARCH METHODOLOGY
Since the topic of earning management or accounting manipulations is to some extent controversial over which management of any company avoid to comment, thus secondary data is used for present study and website of journals from SSRN, DOAJ, and websites of India forensic, Directors database, SEBI, MCA and ICAI will be the prime sources four secondary data.

Research Design: Exploratory research will be used in present paper, it will draw definitive conclusion with extreme caution and with its fundamental nature, it will try to conclude the probable existence or non existence of problem.

Structure: The paper is divided into four major sections; section one will describe brief meaning of earning management and reasons behind it with literature review; section two will consist of various facilities companies get from regulations to get into earning management practices; section three will examine ethical dilemma on good or bad side of managing the earnings and last but not the least section four will draw a attention of government or regulatory bodies towards the probable challenge for Indian corporate from such accounting manipulations.Paper is however more of descriptive in nature thus the conclusion drawn will give a scope for future research.

LITRATURE REVIEW
The concept of earning management is new in country like India but the practices followed are very common and attracting many scholars to work on various facts and issues related to earning management in future growth and development of Indian economy. There are studies available on relationship between good governance and less financial fraudulent reporting (Beasley 1996; Abbott. Parker and Peters 2000) but very less research is available on dramatic case of earning management.

Earnings management (EM) is an accounting practice which, it is argued, is used to represent the financial situation of a company realistically. The accounting literature reveals that EM is mainly undertaken with the following intentions: to represent the 'true' value of a firm; to mitigate information asymmetry; managerial concern towards incentives and job security; to reduce cost of capital, social and political costs, agency cost; for strategic reasons (e.g., mergers and *acquisitions); impression, reputation and/or relationship management; internal aspects of organizations (e.g., competing managers attract resources on the basis their superior performance. (Siddharth Mohapatra, 2011)*

Sonda Marrakchi (2001) in his study investigated the relationship between governance, publicly available information and earning management and examine that whether firms' corporate governance practices have an effect on the quality of its publicly released financial information. The findings suggest that earning management is significantly associated with some of the governance practices by audit committees and board of directors. He also gave evidence that effective board and audit committee is a constrain for earning management. Similar to Marrakchi findings and consistent with Beasley (1996) it was also found that experienced and knowledgeable independent board decreases the probability of high earning management. There are many scholars who have worked on disclosure practices of different firms and one of such study indicate that there is negative relationship between firm disclosure practices and earning management, it is observed that earning management arises from information asymmetry, which can be minimized through proper disclosure system.Gerald J. Lobo &Jian Zhou (2001) used rating published by the Association for Investment Management and Research to measure corporate disclosure, and discretionary accruals from the modified Jones model to measure earnings management. Consistent with theoretical predictions, the empirical analysis indicates that there is a statistically significant negative relationship between corporate disclosure and earnings management.

Disclosure practices are not yet clearly defined and investors are not well aware whether the information disclosed is full and relevant for investment decision. In India there is only one source whereby stakeholders can have information about the financials of the company i.e. financial statements or auditor report. However, the manner in which those statements are prepared and the kind of judgments mangers have used in recording the transactions are not disclosed properly and even the information which is easily available and are provided under legal rules to the market is not properly utilized or assessed for taking investment decision.

Recent study conducted by Imen Fakh fakh (2010) has shown that earning management is the result of CEO compensation. When the compensation or incentive of managerial personnel is based on performance of the company, the probability of earning management or manipulations in accounts are more. It is however observed that earning management is not easy to remove from the system as it is based on judgment and management discretion and thus in order to get more incentive favorable judgments can be made in taking decision. It is also seen that regulatory bodies have tried in taking steps to protect statements from such malpractices but due to lack of moral and ethical values, such norms could not support the objective.

One of such step is taken by US in enacting Sarbanes Oxley Act 2000 and Clause 49 of listing agreement in India which are proven very successful in minimizing earning management. Findings suggested that regulatory intervention through the implementation of SOX reduced the practice of earnings management (Rachel Ang, 2011).

Enhancing the role and importance of auditors and independent directors (Clause 49) again depends upon their moral and ethical values. Indulging in wrong practices is possible even through independent nature of directors if they are also involved in incentive based motives. Board plays an important role in minimizing such practices and in order to analyze their importance in providing ethical picture of firm, four broad characteristics are examined; board size, independence, motivation and competence (Sonda Marrakchi, 2001) in analyzing the role of board in minimizing earning management and it was found that larger the board size there will be less probability of working effectively. Adequate number and quality board can help in reducing earning management practices.

The essence of theories conducted on earning management does not lie in the meaning of earning management only. Theories have focused on the practices followed by major corporate in India and other developing countries within the purview of system. Efficient board, effective governance system and well defined disclosure system of any company can minimize the probability of higher earning management. Performance based incentives are considered as major reason of earning management and therefore needs to be regularized. Any improvement in performance of company should be properly checked and sources of better performance in terms of profit or revenue should be examined properly.

MOTIVATION FOR EARNING MANAGEMENT

REASONS OF EARNING MANAGEMENT

In spite of many regulations and prevention steps such practices are not completely removed due to the nature of transactions. One can not take action against use of particular method of accounting if that method is approved and allowed by regulatory bodies itself.

Secondly, investors are not well aware and informed about the concepts and methods of accounting and finance and thus mostly rely on expert knowledge and advices. This is one of the major reasons of increasing number of earning management practices. Team effort of management of company and financial advisors sometimes lead to personal gains at a cost of investors' losses.Secondly, information asymmetry is another reason these days and many scholars have considered it as major motivational factor of manipulations. Dye (1988) and Trueman and Titman (1988) show analytically that the existence of information asymmetry between management and shareholders is a necessary condition for earnings management.

In case of performance based incentives and pressure of achieving the targets it becomes a necessity for the management to mould the books in the way it is desired.

The solution for minimizing the gap in information available with stakeholders and managers is awareness, which is facilitated by rights provided to public by regulatory bodies. But many investors are not accessing those rights and depend upon market to react. Although numbers of studies have been conducted on information asymmetry and major findings, suggest that the probability of occurrence of earning management will be more in companies having less disclosure practices (Gerald J. Lobo**)**. The problem in system is, different people knows different things but no one knows everything and in such a environment a managed earning stream can convey more information than an unmanaged earning stream. (Arya, Glover & sunder)

Apart from performance based incentive and personal profit making objective, there are other motivations also which have never been considered in studies conducted on aggressive accounting or earning management, such as flexibilities provided by regulatory bodies and lack of knowledge about accounting or financials of company among investors.

It has also been observed that there is no clear solution of earning management or aggressive accounting as the line which can differentiate fraud and aggressive accounting is not clear and usually depends upon judgments. And hence presence of judgment in system is motivation of earning management. Another most important motivation is competition which forces management to indulge in managing the books in most profitable form at the cost of its truthiness' as happened in Xerox decade ago. Through an open discussion with auditors and accountants, it was observed that earning management is always appreciated by the management and accountants are asked to manage the earnings in desired way. Such acts are usual course of business and are considered as regular duty of accountants. Many believe that there is nothing wrong in utilizing the best possible alternative available in system unless bad intentions are clear. If the interpretation of such an act misrepresents financials of the company and there is no scope of questioning management, investors or analysts will be helpless, thus there is strong need of understanding and clearance what is right and what will be wrong.

Some of the earning management techniques available in system and duly allowed by regulatory bodies are as follow:

- Alternative method of inventory valuation such as LIFO, FIFO and average inventory pricing method
- Cooking Jar reserves are created by companies through recording more expenses in current fiscal period to make it possible to record less in future period and they can tap into later to get an earning boost.
- Creating special purpose entity as happened in Enron Ltd. where assets are transferred to SPE by the means of sale and gain or losses are shown in books
- Revenue and expense recognition techniques
- Using more of derivatives
- Transfer pricing techniques: Transferring goods to inflated market to increase the profits or buying goods from deflated market is another technique of producing desired results.
- Showing unexpected gains or losses from long term assets which were shown on cost

EARNING MANAGEMENT-GOOD OR BAD

There is no clear definition of earning management and can not be considered as fraud thus it is very difficult to decide whether earning management is good or bad. Selecting the best method of treating any transaction is not bad and should be appreciated for managing the books effectively. But when one method is misrepresenting the financial position of firm and giving wrong impression in the mind of investors or public at large then such practice should be considered as bad. But here the detection of intention or motivation of management to indulge in such practices is not easy job and require detailed information about the working of accounting practices.

Earnings management can be useful for shareholders if it is used to inform stuffs not included in the company's financial report. Some researches support this statement and called it beneficial earnings management (Subramanyam, 1996). There are situations where particular practice do not affect negatively to either management or investors but can misinterpret the financial position. Common example is maintaining high level of reserves in case of good financial position, such transfer of profit in reserves will reduce the earnings and analyst may get wrong impression of less earning in that particular time period.

Company can justify the reason of transfer of profits in reserves, to consider such treatment of profit as ethical and effective earning management. It can give justification on requirement of reserves in future for e.g major projects in pipeline or some future investments etc. But if decision of transfer of profit to reserves are done without any future requirement or need then it may be assumed that company wants to hide its profits from higher corporate taxes. Although hiding profits from taxes may be beneficial for investors, too in short run but socially and legally it is unethical and illegal. Thus the decision on good and bad of earning management depends on motivation and intentions to adopt one particular method of treating the transaction.

There is no doubt that company can get short term profits from earning management practices. If a company follows any technique which shows higher fictious revenue and in result of which market image of the company improves then existing shareholder seeing the higher prevailing market prices can sell their shares and go out of the market in good time but on the same side it is bad for prospective buyers and long term sustainability of firm.

Ignoring the fraud part in managing earnings if firm transfer some part of expenses or losses from one unit of business to other then such practices are consider as smart act on part of management. In many cases companies in order to be competitive eliminate or restructure the subsidiaries and estimate the cost of this change against current earnings. Estimating higher end of such change may give negative impression to the market and market price of share may fall down and if company selects lower end side of cost then future high expenses may again affects the image. In such situation it becomes the management discretion to decide which method is better for firm's image and performance. Such management of earnings is well invited and appreciated by the corporate and experts try to spend plenty of time in deciding in favor of firm.

Another most popular technique is creating special purpose entity and sell of loss making assets or non performing assets to SPVs. The profit or loss on sale is shown in transferor's accounting books and removing such assets from the books improves the face of transferor books of accounts. The accounts of such SPEs are not consolidated with transferor and thus its effect can be hiding from market. Under such situation the objective of creating SPE is to remove non-performing or loss making assets from the books and the purpose is neither harming the image of firm nor the investors' interest. Till any management of earning technique harm the value system of firm or affect the interest of investors, such practices should be consider as good practices.

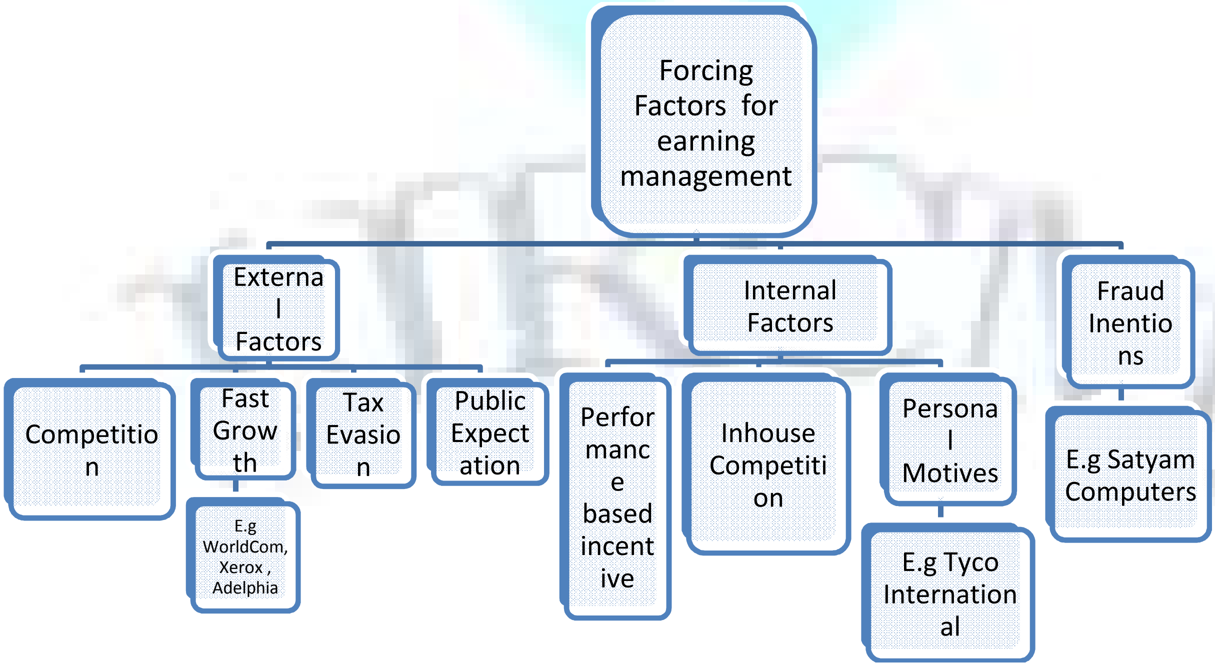
Hanna (1999) stated in his article that management in order to put more earnings in the bank tempted to provide excessive unusual, non recurring and extraordinary charges. Hence, it becomes difficult for stakeholders to understand the reason of increment in earnings. It has also been observed that most of earning management occurred at the time of IPO where by investors are ready to pay unrealistic price for shares. Teoh et al. (1998b), using annual accounting information, find that earnings management around the IPO are higher for issuing firms as compared to non-issuing firms.

PROBABLE CHALLENGES FOR INDIAN CORPORATE FROM SUCH ACCOUNTING MANIPULATIONS

A responsible earning management practice is good for corporate as well as investors because unmanaged earning do not generate perfect figures always. For the management of books effectively it is important to use innovative way of managing them but it should not be used aggressively. Corporate have very well adopted innovative ways of managing their books of accounts, many technological based updation have been made in managing the books which is good enough for running the business efficiently and can help in long tem sustainability of firm. Another mode of managing books is also prevalent in various giant firms i.e. managing the books in aggressive way. Although there is nothing wrong in managing accounts in ways suggested by accounting system such as following any alternative method of accounts preparation is legal and smart practice but following alternative way of managing the books just to mislead the stakeholders and getting undue advantage from it should be avoided and can lead to short life of the company.

Companies are also in favor of ethical accounting but the internal and external pressure pushes management to manipulate the books. Figure-1 below shows factors which forces companies to indulge in earning management practices:

FIG. 1: MOTIVATIONAL FACTORS



WorldCom, Enron, Adelphia and many more such big name in creative accounting and earning management cases were under external pressure i.e. competition and fast growth in the industry. Satyam Computer was the third factor i.e. fraud intention which forces management to follow creative or earning management practices.

Problems or challenges may arise for those honest firms which are following ethical management practices. The act of WorldCom might have vanished many growing companies by giving them strong competition. Market was not aware about the wrong doing of Satyam Computers before 2009 and those competitors who were performing well and were following ethical practices could not make better image or positive image in the mind of investors due to facing strong competition from Satyam Computers. Fraudulent practices followed by Satyam Computers became a constraint in the growth of its competing firms.

Earning management can be a constraint in growth and development of companies in any country in two ways first, it spoil the image of economy and affect the long term sustainability, second, it hinder the growth of small and growing firms. Secondly, corporate have to make an effort to convince stakeholders that they are following ethical practices. In highly competitive market corporate are forced to spend their quality time and money in implementation of ethical practices. This creates a road block in growth and development of corporate. It is however observed that such problems cannot be removed from the system as it is personal moral values which guide the person about right and wrong.

Economy never allow any citizen whether person of corporate to enter into any unethical practice even if it brings profits for the country. Companies keeping in mind the importance of ethical business have started realizing that the main aim of any business should be sustainability not profitability. And sustainability should not be at the cost of company's image. We have seen that companies in order to fulfill this objective are following unethical practices so that they can be competitive and can survive in the market. Major challenge for corporate is to be competitive as it is consider as only way of ensuring sustainability. It has also been argued that ethical business can not be possible fully as it depends upon moral and ethical values of individual too. Companies while recruiting people can not ensure fully whether selected person has good moral and ethical values. And secondly, many of our accounting standards depend upon judgment of decision maker. Thus many of studies have concluded that there is no perfect solution for earning management or creative accounting.

Concept like social responsible investing and ethical investment are introduced to promote ethical culture in society. Investors are advised to invest in ethical firms and in promoting same there are ethical funds available in mutual fund. Taurus Ethical Fund from Taurus Mutual Fund is India's First Actively Managed Equity Oriented Shariah Compliant Diversified Fund.It allows a socially responsible form of investing and offers adequate diversification. But unfortunately investors hardly know about such funds floating in the market. And those who knows consider them as secondary investment option as these funds are still not consider as profitable investment options. There is a need of generating such a system where awareness becomes mandatory for all investors before investment decision. However there are investors' protection and awareness program available but due to lack of understanding of financial aspects and importance of analysis before investment, such protection programs becomes handicap. Thus this is another challenge for government to design a proper system which can ensure that market is fully aware about services and rights available to them.

When corporate tries to indulge in any unethical practices, regulatory bodies' vows to remove flaws from the system and ensure to provide safe market for investment but moral and ethical values of individual sitting in responsible positions in reverse inhibit the system to let corporate in producing the desired results in unethical ways. Thus in spite of various norms and protection initiatives of government, such practices can not be removed completely from the system.

CONCLUSION

Earning management is art of managing the books, utilizing the alternatives available in accounting system in best practice. Such management of earnings can be ethical or can be unethical depends upon intentions and aim of following any particular method. There are studies conducted on justification of earning management practices and it has been observed that such practices are not bad unless the real intentions are clear. There are alternatives available in accounting system and selecting one method to manage the earning in better way is consider as smart practice. But on the similar side if such practices are followed to produce desired results by showing false numbers are consider as unethical and immoral.

One can not predict or assess the transaction whether it is good or bad the only option available is to keep a check on movement of numbers and methods. What method is adopted, when did it changed and the reason of change and most important is what the impact of such change on financials is. Although various techniques have been found out by studies which can give an idea of unethical accounting practices such as creating cooking jar reserve, more use of derivatives, adopting one method of inventory valuation which provide desired results and creating special purpose entity to transfer transaction which company don't want to show in its books.

Gone are the days when companies aim to earn profits, today in highly competitive market all the companies are aiming to sustainability and in order to sustain in the market, various practices are followed which are helping them in fulfilling the sustainability objective. There are evidences of long term sustainability through wrong practices also. Enron, Satyam and WorldCom were the major example of how they have achieved the objective of competing in the market though manipulations. From practices like earning management, creative accounting or aggressive accounting these companies could compete in the market for long. There were number of competing firms who could not compete because of growth of those firms which were following wrong practices. Such practices help them in attracting large number of stakeholders and hence growing and new companies could not sustain for long. Thus this becomes a challenge for government and regulatory bodies to find out the solution for honest market players. Corporate needs to understand the importance of ethical practices and should accept that unethical practices results only loss of business and brand name. Investors who doesn't stay in one company may gain in short period from such companies but market as a whole may face lots of problems if no adequate steps are taken to prevent the corporate. All the sectors of economy are related in one of other way and thus fault on one part of economy affects all other sectors. Thus there is strong need of proper system whereby safety in investment in financial market can be ensured.

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