

# **Analysis of the Relation between Conservatism and the Amount of Dividends Payable to Shareholders. The Case of Romanian Listed Companies**

Claudia-Cătălina Ciocan  
„Alexandru Ioan Cuza” University of Iasi,  
Faculty of Economics and Business Administration  
[ciocan\\_claudia\\_catalina@yahoo.com](mailto:ciocan_claudia_catalina@yahoo.com)

## **Abstract**

*This paper has as a main purpose to identify if the use of provisions in accounting is able to produce significant changes in the amount of the distributed earnings (dividends) for the Romanian listed companies. For this purpose, we compute a correction of the distributed earnings by excluding expenses and revenues reported for provisions while maintaining the dividend payout ratio at a constant level. The results indicate significant differences between the dividends actually paid and the potential dividends obtained by excluding the effects of the provisions recognition. We conclude that the use of conservatism in order to avoid decapitalization is a real fact for the company even though the investors seem to be placed in the background. Also, the paper aims to identify and systematise the reasons that should lead the management to recognize provisions in accounting despite the impact exerted over the dividends payable.*

**Key words:** provisions, conservatism/prudence, dividends, decapitalisation, risk

**J.E.L. classification:** M41

## **1. Introduction**

In the context of the continuous evolution of the economy, both at national and international level, an important element to be considered is the risk. This is an extremely known concept and by understanding it it's possible to explain the success or economic failure. The development of all businesses is under the mark of risk, and its approach makes the business a resounding success or a lamentable failure. At management level a wrong approach or risk avoidance can lead to alteration of the managerial process, the company being unable to effectively cope with various exposures to losses. Given that management bases its decisions on financial and accounting information, it should be seen to what extent this information describes the risks that threaten the company.

In order to see how the risk is dealt with in economic theory and practice, we decided to focus on the use of *provisions* which, in this case, can be considered instruments of anticipation and protection against negative events that can generate losses for the company and whose recognition is intimately linked with accounting conservatism (Feleagă, Dragomir and Feleagă, 2010, p. 6).

The paper is divided in the following way: section two presents the theoretical background, introducing provisions and the reasons that should lead managers to recognize them, the third section presents the conceptual delimitations of conservatism and its relation with provisions, the fourth section presents the methodological approach followed by the results and discussions section and the last part presents the conclusion.

## **2. Theoretical background**

To get to the reason for using provisions, we must first talk about the risks and how they are addressed in line with *true and fair view*, considered by international accounting practice an overriding concept, that takes precedence over all other legal provisions (Van Hulle, 1997;

Alexander and Archer, 2003) and **conservatism**. When it comes to risk, we have to admit that it is a factor present in every moment of our lives, whether we are walking down the street or we decide to invest our savings. Risk is everywhere and is both the most interesting and exciting challenge, precisely because of its presence in both the social and business spheres, in all areas of activity. We can argue with certainty that the main goal of a business is to achieve positive outcomes/ profit. Either way, achieving this goal can not take place in the absence of potentially loss-making events. According to Lam (2014), running a successful business involves pursuing the opportunities that come with the financial and managerial capacity of society by taking risks.

The concept of risk is defined in the literature in several directions: „*an uncertainty affecting the outcome*”, „*the likelihood that the actual outcome will differ from what is expected*”, „*the possibility that losses are greater than initially estimated*”, „*uncertainty about a disaster*”, all of these definitions starting from a common element, **uncertainty**. Uncertainty/insecurity in the economic environment can arise from two sources:

- the unpredictability of economic processes that reflects the objective nature of risk;
- the lack of essential information that reflects the incomplete character of information published by companies.

Until recently, the definition of risk included only the negative side, the threats it implies. At the beginning of the 21st century, the definition of risk marks a change of mentality in terms of its components. So new definitions emerged, which included both the negative side and the positive aspects that accompany this concept. In light of the occurring changes, a proper definition of risk can be considered „*an uncertain event or condition that, if occurs, has a positive or negative effect on the target set*” (Project Management Institute Inc, 2000).

There are numerous classifications for the risk, depending on the areas, the activity and other criteria proposed by the extensive literature regarding risk management. The most representative for accountants involves:

- contractual risks - caused by the lack of liquidity, which leads to the impossibility of paying the debts at maturity. According to Neacsu (2018), this risk can occur either when a contract is no longer of interest to the partner (risk of failure) or a partner is unable to meet its contractual obligations (risk of insolvency).
- financial risks - generated by changes occurring under market conditions. These risks are beyond the control of the company and directly affect its results.
- taxation risks - mostly generated by changes occurring in the tax laws of a country. Some examples that have made the mark on the Romanian business environment are: the increase of the limit to which a company may pay tax on the income of microenterprises, the reorganization of social contributions, the 10% tax on personal income, the increase of the gross minimum wage and the new system for paying VAT, all applicable from 1 January 2018.
- legal risks - generated by possible loss of income due to penalties, fines the company is liable due to non-application or misapplication of contractual / legal disposition or by inappropriate establishment of the obligations owed by the state (Moinescu and Codirlasu, 2009).

Companies need to realize their vulnerabilities, to reconfigure their strategies, to identify ways to break out of potential crises and mitigate losses. All these factors have led executives to propose a series of solutions: *preparing plans with solutions for the „worst case scenario”, under the current conditions of accelerated declining growth, a concrete orientation towards cost reduction and increase of cash inflows* and last but not least, **a realistic and balanced assessment of contractual, financial, fiscal and legal risks**, especially for countries where the taxation system is unstable (as is the case for Romania). Probable losses may be known, reasonably estimated, or not, and hence **the estimated amount of the provisions**.

Provisions can be considered an accounting tool used to anticipate and manage business risks. The pertinent question is „*what is the maximum level to which we can be cautious?*” Because conservatism prevents exaggeration with the purpose of overvaluing assets or understating debts and also does not involve the creation of secret reserves, overvalued or facade provisions. In order to answer this question, we must look at conservatism through a relationship of subordination with the true and fair view concept. This concept symbolises the quality of the information provided by a company, in terms of fidelity and sincerity, namely a clear, real picture without influence from

the information producer. Or, the relationship between the two concepts can often be considered conflictual, because by using conservatism we get a pessimistic picture of the business, a picture that lacks neutrality. In most cases, shareholders require less prudent accounting information, because they are interested in the company's ability to pay dividends, and creditors prefer conservatism, because influences the results in terms of their reduction, avoiding this way the distribution of unrealistic earnings through dividends. The two concepts appear again in antithesis because at international level, true and fair view is a highly used one, being in fact a basic principle of accounting. Nationally, however, it does not enjoy this recognition, true and fair view being noted more at a theoretical level than the practical one. The same cannot be said about conservatism which, although it is left in the background at international level, at national level, occupies a privileged place, even overriding the other principles.

The issue of reporting provisions in the financial statements also makes a mark in comparing the two concepts. Feleagă et al. (2010, p. 2) state that the accounting theory predicts the alteration of the true and fair view through the abusive use of provisions. Therefore, we can say that exaggeration, the abuse, the creation of hidden reserves and oversized provisions is able to distort the true and fair view of the results of a company. The use of provisions based on realistic estimates of required expenditure, appreciated by the entity's management, supplemented by the experience of similar transactions and in some cases by reports prepared by independent experts of the entity (Feleagă, Dragomir and Feleagă, 2010) may place conservatism as a complement of true and fair view. The situation can be addressed from two perspectives:

- „*why should we report provisions?*” Reporting provisions in this case would lead to transparency in the business environment, to qualitative information that would lead investors to a sense of security, to a complete and faithful representation of the business. They would see that the company respects moral values and will thus be protected in the future. On the other hand, risks also arise because shareholders are interested in dividends, and their reporting diminishes it. These situations lead shareholders to raise questions: „*Are the provisions really necessary or are they used in order to justify the reduction of the earnings and dividends by default?*” Also, the risk may also occur for potential investors, who are ultimately interested in the same thing as the shareholders: dividends. In addition, the non-inclusion of provisions in the financial statements in a consistently manner may raise questions about the sincerity of the information provided through financial reports.
- „*why should we not report provisions?*” A company would be tempted not to include provisions in financial reports as they could lead to a negative image vis-à-vis to creditors, current and potential investors and other users interested in the company. Lenders can ask for their loans to be covered within a shorter period of time, which would destabilize the company's liquidity and increase long-term indebtedness. Certain provisions, such as for litigation or onerous contracts, raise questions to investors and shareholders about the company's business, which poses new risks to the entity, the risk of losing shareholders or new investors.

However, whether we report provisions or whether we decide not to, one thing is certain: the risk is present and unattainable in this equation. Conservatism, in this case, complements the construction of the true and fair view because the estimation of the economic downturn of the negative events that took place only completes the overall picture of the company's results. It is up to each accountant to decide whether to take into account the signs that arise and which require their transposition into accounts using provisions. This reasoning is necessary especially in the context of the current economic and financial crisis where quality information leads to future economic benefits and the lack of it or using it improperly could lead to the loss of these benefits or even bankruptcy (Robu, 2014).

### **3. About conservatism and its relation with provisions**

The explanatory dictionary of the Romanian language defines prudence as the assimilation of a person to be far-seeing, circumspect or cautious. When prudence is used in a colloquial sense, it is associated with self-protection, the relationship between the two being almost tautological. This association is maintained as well, at the conceptual level, in accounting but it lags behind the

seemingly negative consequences of recognizing potential losses using provisions. From an accounting point of view, conservatism (prudence) is defined by accounting regulations as the impossibility to recognize asset increases or debt reduction (OMFP No. 1802/2014), while some authors define it as the difference between economic value and net book value (Barker, 2015; Tracey, 2015). Maltby (2000, p. 52) identifies three overlapping but distinct meanings of prudence. The first and oldest related to prudence as a moral virtue conducive to honesty and competence in business. The second meaning, which became current in the nineteenth century, was the conservation of capital through the avoidance of over-distribution and the third sense of prudence was associated with creative accounting. According to the author, the 20th century prudential discussions are organized around two opposite principles: a belief that prudence is irrelevant because leads to understatement, and a commitment to it as an indispensable tenet of accounting. The significance of prudence, as suggested by the author is not fixed and immutable, but has evolved along a path that has progressively aligned it with the interests of social capital. The change was a gradual alignment of prudence with investor interests. It ceased to be a general moral virtue and became a specific economic one, characteristic of the successful businessman. Basu (2001) puts into question the issue of the definition and measurement of prudence and reconciles some previous findings with regard to differences in prudence between countries. The author presents the concept as denoting accountants' tendency to require a higher degree of verification to recognize good news as gains than to recognize bad news as losses (Basu *et al.*, 1997, p. 7) and states that it is necessary to distinguish between the balance sheet and income statement effects of conservatism, since they do not always go „hand in hand” (Basu, 2001, p. 1335). Gox and Wagenhofer (2009, p. 2) contribute to the understanding of the economic roles of conservative accounting and provide an economic reason for why asset measurement is conditionally conservative, or, more precisely, why unfavourable information is recognized by an impairment of the book value of assets whereas favourable information is not recognized. The authors point out, using an investment model in a risky project, that in the absence of any accounting regulation, a firm seeking to fund a risky venture capital project will optimally design a conservative accounting system.

One of the roles that can be attributed to financial reporting is to reflect management's ability to maintain capital and reward investors by providing dividends. Therefore, cautiously addressing the profit is to mitigate allocations from a non-existent or insufficient profit, as well as to prevent cash-flow outflows. The financial statements prepared according to the accounting regulations in force reflect the past activities of a company, taking into account two dimensions: quantitative and qualitative. A first dimension, the quantitative, takes into account the figures resulting from the accounting processing and which represents the financial position and the performance of the entity (Berheci, 2010). The second, the qualitative dimension provides interpretations of the abovementioned figures, usually in the notes to the financial statements describing the used methods and other additional information. In the financial statements, *provisions* are recognized as liabilities and are expensed to cover future losses that are probable at the end of the year. Therefore, they affect both the financial position and the performance of the company. According to *IAS 37 Provisions, Contingent Liabilities and Contingent Assets* the recognition of a provision occurs when (a) an entity has a present obligation as a result of a past event; (b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and (c) a reliable estimate can be made of the amount of the obligation (IFRS, 2017). No provision for future operating losses is recognized because these future losses do not meet the definition of a liability and the criteria for recognizing provisions (MFP, 2014). Feleagă et al. (2010, p. 7) state that because the entity can avoid the future expenditure by its future actions, for example by changing its method of operation, it has no present obligation for that future expenditure and no provision is recognized.

Recognition of provisions in the financial statements is a result of the application of the conservatism. But it is considered that their use creates an asymmetry in accounting: *on the one hand, a company cannot present asset value increases or decreases for debts, even if they are obvious, but it is required to record all negative trends in accounting, even if they are estimated.* By ignoring potential earnings, the company protects its stakeholders from the risk of being ... optimistic and by recognizing provisions discloses information about events that can generate

losses for the company. Watts (2003) explains that the contracting explanation of conservatism suggests that accounting is a means of addressing information asymmetry amongst the various parties to the firm. In practice, accounting conservatism defers reported earnings and understates net assets, thus constraining opportunistic wealth transfers by management at the expense of other parties.

#### 4. Research methodology and data

Toma (2001) states that conservatism seeks to provide a safety margin for the company and users of financial information. It protects tomorrow's owner from an expense that belongs to today's owner and avoids decapitalization of the firm, which may occur in response to the distribution of unrealistic earnings (Horomnea, 2013, p. 258). The same assertion is supported by Montesinos et al. quoted in Machado Cabezas (1996, p. 811) and Maltby (2000, p. 52). It can therefore be concluded that the purpose of conservatism is to protect the wealth of a company against the risk of reflecting oversized earnings, the distribution of which could lead to the company's decapitalization. Neag and Adorjan (2016, p. 136) assert that *provisions*, which can be considered an accounting tool used to anticipate and manage business risks, directly influences the calculation of the distributed earnings. Thus, starting from the model proposed by the authors, we sought to identify the impact exerted by the non-recognition of the provisions over the dividends and in order to do so we analysed the change in the amount of the dividends ( $\Delta Div$ ) considering the paid dividends and the corrected ones as follows:

$$\Delta Div = \frac{Div_{corrected} - Div_{paid}}{Div_{paid}} \times 100$$

Where

$\Delta Div$  is the change in the amount of the dividends

$Div_{paid}$  the paid dividends according to [www.bvb.ro](http://www.bvb.ro)

$Div_{corrected}$  the corrected dividends resulting from the corrections applied over earnings per share ( $EPS_{corrected}$ ) in line with the formulas:

$Div_{corrected} = (R_{div} \times EPS_{corrected}) / 100$ , where

$R_{div}$  represents the Dividend Payout Ratio =  $(Div_{paid} / EPS) \times 100$  being considered a constant in the analysis

$EPS_{corrected} (1) = [(Net\ Income + Expenses\ reported\ for\ provisions) / Outstanding\ shares] \times 100$

$EPS_{corrected} (2) = [(Net\ Income + Expenses\ reported\ for\ provisions - Revenues\ reported\ for\ provisions) / Outstanding\ shares] \times 100$

Dividend payout ratio indicates the percentage of earnings paid to shareholders in the form of dividends. The closest to 100%, the higher the share of the profit for the dividend's payment (Neag and Adorjan, 2016). This rate is constant.

To reflect the extent to which provisions affect the size of dividends, we recalculated the **dividends** and the **earnings per share** considering two options: one in which the estimation of these indicators take into account only the income and expenses reported for provisions excluding the revenues reported for provisions (results presented in Panels A - section 5) and one in which we included both expenses and revenues reported for the provisions (results presented in Panels B - section 5).

Unlike Neag and Adorjan (2016), which adjusted the paid dividends using only the value of the reported provisions, the present paper uses the expenses and revenues reported for provisions, for the recalculation of earnings per share ( $EPS_{corrected}$ ). We consider that this correction is much more appropriate because it includes only the effects produced in the analysed financial exercise. As reflected in the balance sheet, the reported provisions include, in addition to the estimates attributed to the current period, the value of the estimates made in previous years, thus leading to over-sized corrected dividends for each analysed exercise. Considering the explanations given by Basu (2001, p. 1335) concerning the distinction between the effects of prudence on the balance sheet and income statement and the fact that the profit is calculated as the difference between revenues and expenses, by limiting only to the information in the income statement, we eliminate the

shortcomings created by the use of provisions in the calculation of the corrected dividends.

The analysis includes a total of 64 companies listed on the Bucharest Stock Exchange (BSE) on the Standard and Premium tier. From a total of 87 listed companies registered in 2018 we excluded some companies as follows:

- 12 financial institutions, financial investment institutions, mutual funds and other similar financial entities;
- 11 companies for which it was not possible to collect data for the analysed period.

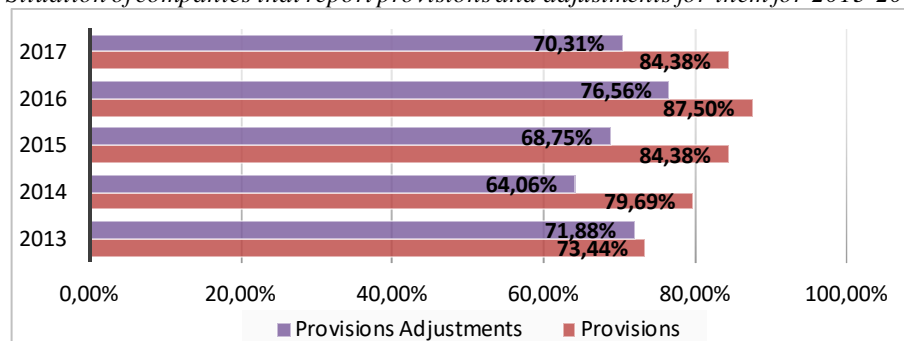
The data for the analysed variables were collected from the individual financial statements of the companies reported in accordance with IFRS. The time horizon considered was the 2013-2017 period. The primary source of data collection was the [www.bvb.ro](http://www.bvb.ro) site and in some cases (either due to the unavailability or to confirm the data) we visited the websites of the analysed companies. For each year, all 64 enterprises were counted thus totalizing 320 observations.

## 5. Findings

The Romanian business environment is an unstable one and is at an early stage in attracting financing through stock exchanges. Romania is also a country where small companies and microenterprises, are predominant. As Burlacu (2017) pointed out in the situation presented at the CAFR (Chamber of Financial Auditors from Romania) congress, Romanian SMEs accounted in 2017 for 99.91% of all enterprises active in the national economy. Microenterprises registered a weight of 97.8%, small enterprises 1.7% and medium enterprises 0.3%. These are companies to which the general public does not have access to financial statements, companies that have no legal obligation to audit the financial statements. As provisions are not mandatory, but are a voluntary component that involves using professional reasoning to estimate uncertainties, for some small companies, we dare to say that for most of them, they are not a priority either because the risks are too many and difficult to estimate, either because accountants do not consider it necessary to use them or do not know how. In the process of collecting data from the financial statements we found cases where the depreciation of current assets (especially adjustments for bad debts) were recognized erroneously as provisions. Transparency required by users is not a primary objective for companies, especially for small ones. *Should investors be aware of all the details, all the risks faced by the entity in perspective, or is it preferred a higher and more attractive income for this category?* The answer to this topic may be different from one company to another.

It can be seen from Figure 1 that, within the analysed sample, the proportion of companies reporting provisions (according with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*) oscillates between 73.44% in 2013 and 87.50 % in 2016. At the same time, the proportion of those who report provisions adjustments (expenses and/or revenues reported for provisions) oscillates between 64.06% in 2014 and 76.56% in 2016. Given that the analysed companies are predominantly big ones, that are submitted to external audit and their reports are public for existing and potential investors we can state that reporting provisions in this case is designed to ensure a higher degree of transparency regarding risk management.

Figure no. 1. Situation of companies that report provisions and adjustments for them for 2013-2017 period



Source: Author's own processing

From table no. 1 it can be seen that out of the 64 companies analysed for the 2013-2017 period only a part of them paid dividends. Also, the further analyses will exclude the cases in which the companies paid dividends but there were no provisions adjustments, since these results will not be relevant leading to no changes in dividends.

Table no. 1 Companies that granted dividends during 2013-2017

| Year | Companies that paid dividends |         | Companies that paid dividends and reported expenses reported for them |         | Companies that paid dividends and reported expenses and/or revenues reported for them |         |
|------|-------------------------------|---------|---|---------|---|---------|
|      | Valid                         |         | Valid   |         |   |         |
|      | N                             | Percent | N   | Percent | N   | Percent |
| 2013 | 22                            | 34.4%   | 15  | 23.4%   | 17  | 26.6%   |
| 2014 | 29                            | 45.3%   | 21  | 32.8%   | 22  | 34.4%   |
| 2015 | 27                            | 42.2%   | 20  | 31.3%   | 20  | 31.8%   |
| 2016 | 32                            | 50.0%   | 25  | 39.1%   | 28  | 43.8%   |
| 2017 | 30                            | 46.9%   | 23  | 35.9%   | 25  | 39.1%   |

Source: Author's own processing using SPSS 23.00

The purpose of the paper is to determine whether the use of provisions is likely to lead to a significant change in the earnings distributed to shareholders in the form of dividends. In order to do so, we considered the paid dividends during 2013-2017, we calculated the earnings per share, the dividend payout ratio and we adjusted the first two according to the expenses and revenues reported for provisions.

Table no. 2 Changes in dividends

| Panel A: Companies that paid dividends and reported expenses reported for them |                                  |             |         |                                  |                 | Panel B: Companies that paid dividends and reported expenses and/or revenues reported for them |             |         |                                  |                 |  |
|--|----------------------------------|-------------|---------|----------------------------------|-----------------|--|-------------|---------|----------------------------------|-----------------|--|
| Year   | Statistic                        | Std. Error  | Year    |                                  |                 | Statistic  | Std. Error  | Year    |                                  |                 |  |
|  |                                  |             | Mean    | 95% Confidence Interval for Mean | 5% Trimmed Mean |  |             | Mean    | 95% Confidence Interval for Mean | 5% Trimmed Mean |  |
| 2013   | Mean                             | 48.02%      | 22.47%  |                                  |                 | Mean   | 9.50%       | 8.53%   |                                  |                 |  |
|  | 95% Confidence Interval for Mean | Lower Bound | -0.17%  |                                  |                 | 95% Confidence Interval for Mean   | Lower Bound | -8.59%  |                                  |                 |  |
|  |                                  | Upper Bound | 96.21%  |                                  |                 |  | Upper Bound | 27.59%  |                                  |                 |  |
|  | 5% Trimmed Mean                  | 38.55%      |         |                                  |                 | 5% Trimmed Mean  | 4.00%       |         |                                  |                 |  |
|  | N                                | 15          |         |                                  |                 | N  | 17          |         |                                  |                 |  |
| 2014   | Mean                             | 74.46%      | 32.08%  |                                  |                 | Mean   | 39.07%      | 22.35%  |                                  |                 |  |
|  | 95% Confidence Interval for Mean | Lower Bound | 6.88%   |                                  |                 | 95% Confidence Interval for Mean   | Lower Bound | -7.41%  |                                  |                 |  |
|  |                                  | Upper Bound | 142.04% |                                  |                 |  | Upper Bound | 85.55%  |                                  |                 |  |
|  | 5% Trimmed Mean                  | 50.65%      |         |                                  |                 | 5% Trimmed Mean  | 19.77%      |         |                                  |                 |  |
|  | N                                | 21          |         |                                  |                 | N  | 22          |         |                                  |                 |  |
| 2015   | Mean                             | 84.82%      | 35.86%  |                                  |                 | Mean   | 54.89%      | 31.10%  |                                  |                 |  |
|  | 95% Confidence Interval for Mean | Lower Bound | 9.76%   |                                  |                 | 95% Confidence Interval for Mean   | Lower Bound | -10.20% |                                  |                 |  |
|  |                                  | Upper Bound | 159.89% |                                  |                 |  | Upper Bound | 119.97% |                                  |                 |  |
|  | 5% Trimmed Mean                  | 59.86%      |         |                                  |                 | 5% Trimmed Mean  | 33.47%      |         |                                  |                 |  |
|  | N                                | 20          |         |                                  |                 | N  | 20          |         |                                  |                 |  |
| 2016   | Mean                             | 43.16%      | 18.85%  |                                  |                 | Mean   | 6.32%       | 7.92%   |                                  |                 |  |
|  | 95% Confidence Interval for Mean | Lower Bound | 4.25%   |                                  |                 | 95% Confidence Interval for Mean   | Lower Bound | -9.93%  |                                  |                 |  |
|  |                                  | Upper Bound | 82.06%  |                                  |                 |  | Upper Bound | 22.58%  |                                  |                 |  |
|  | 5% Trimmed Mean                  | 25.51%      |         |                                  |                 | 5% Trimmed Mean  | 3.50%       |         |                                  |                 |  |
|  | N                                | 25          |         |                                  |                 | N  | 28          |         |                                  |                 |  |
| 2017   | Mean                             | 18.20%      | 3.84%   |                                  |                 | Mean   | -2.94%      | 7.92%   |                                  |                 |  |
|  | 95% Confidence Interval for Mean | Lower Bound | 10.23%  |                                  |                 | 95% Confidence Interval for Mean   | Lower Bound | -19.30% |                                  |                 |  |
|  |                                  | Upper Bound | 26.17%  |                                  |                 |  | Upper Bound | 13.42%  |                                  |                 |  |
|  | 5% Trimmed Mean                  | 16.88%      |         |                                  |                 | 5% Trimmed Mean  | 2.02%       |         |                                  |                 |  |
|  | N                                | 23          |         |                                  |                 | N  | 25          |         |                                  |                 |  |

Source: Author's own processing using SPSS 23.00

From Panel A presented in table no. 2 it can be noticed that the exclusion of expenses reported for provisions leads to a **positive** change in the amount of the dividends for all of the analysed cases (the interpretation is based on the 5% trimmed mean which is much more relevant considering that the analysis highlighted numerous outliers for the analysed sample). For 2013 it can be seen that the amount of the dividends increases on average by 38.55%, oscillating (as can be seen from Panel A presented in Table 3) between an increase of 3.02% registered by FARMACEUTICA REMEDIA SA and an increase of 263.54% registered by AEROSTAR SA. In 2014, on average, the dividends amount increases by 50.65%, oscillating between a 0.53% increase registered by SOCEP SA and a 586.99% increase registered by OIL Terminal SA. In 2015, the value of dividends increases by an average of 59.86%, oscillating between a 0.39% increase registered by SOCEP SA and an increase of 618.54% registered by COMELF SA. In 2016 the dividend value increases, on average, by 25.51%, oscillating between 0.90% increase registered by T.H.R. MAREA NEAGRA S.A and 472.73% recorded by IAR SA. In 2017 dividend value increases, on average, by 16.88%, oscillating between a 0.61% increase recorded by TERAPLAST S.A and an increase of only 60.05% this time recorded by IAR SA. If we were to consider only the results presented in Panel A without addressing the revenues reported for provisions due to the decrease or use of the provisions, we could argue that the situation of non-recognition of the provisioning expenses is a potentially favourable one for the shareholders who could otherwise be remunerated with more than if they are actually paid.

Table no. 2 Extreme values for changes in dividends

|      |         | Panel A: Companies that paid dividends and report expenses reported for them |       |         | Panel B: Companies that paid dividends and report expenses and/or revenues reported for them |       |         |         |
|------|---------|--|-------|---------|--|-------|---------|---------|
| ADiv | An      | Acronim  | Value | An      | Acronim  | Value |         |         |
|      |         |  |       |         |  |       |         |         |
| 2013 | Highest | 1  | ARS   | 263.54% | Highest  | 1     | IARV    | 137.04% |
|      |         | 2  | IARV  | 248.99% |  | 2     | COTE    | 27.71%  |
|      |         | 3  | ELMA  | 79.59%  |  | 3     | CMF     | 20.94%  |
|      |         | 4  | COTE  | 41.72%  |  | 4     | ARS     | 16.11%  |
|      |         | 5  | CMF   | 22.61%  |  | 5     | CMCM    | 8.46%   |
|      | Lowest  | 1  | RMAH  | 3.02%   | Lowest   | 1     | BCM     | -19.11% |
|      |         | 2  | SNP   | 3.05%   |  | 2     | TUFE    | -17.77% |
|      |         | 3  | PTR   | 3.36%   |  | 3     | ALU     | -13.90% |
|      |         | 4  | SNG   | 3.48%   |  | 4     | SNP     | -11.06% |
|      |         | 5  | SNN   | 3.82%   |  | 5     | TGN     | .33%    |
| 2014 | Highest | 1  | OIL   | 586.99% | Highest  | 1     | OIL     | 460.52% |
|      |         | 2  | ARS   | 378.62% |  | 2     | IARV    | 169.32% |
|      |         | 3  | IARV  | 180.71% |  | 3     | ARS     | 138.42% |
|      |         | 4  | ELMA  | 164.76% |  | 4     | SNP     | 58.89%  |
|      |         | 5  | SNP   | 79.47%  |  | 5     | MECF    | 23.24%  |
|      | Lowest  | 1  | SOCP  | .53%    | Lowest   | 1     | ATB     | -8.97%  |
|      |         | 2  | SPCU  | .61%    |  | 2     | CMCM    | -7.00%  |
|      |         | 3  | ELGS  | 1.31%   |  | 3     | SOCP    | -3.74%  |
|      |         | 4  | EFO   | 1.84%   |  | 4     | BIO     | -2.38%  |
|      |         | 5  | SNG   | 2.54%   |  | 5     | VNC     | -2.08%  |
| 2015 | Highest | 1  | CMF   | 618.54% | Highest  | 1     | CMF     | 529.40% |
|      |         | 2  | PREB  | 356.19% |  | 2     | PREB    | 356.19% |
|      |         | 3  | IARV  | 287.84% |  | 3     | OIL     | 125.93% |
|      |         | 4  | OIL   | 175.54% |  | 4     | IARV    | 42.84%  |
|      |         | 5  | ARS   | 64.53%  |  | 5     | ARS     | 31.07%  |
|      | Lowest  | 1  | SOCP  | 0.39%   | Lowest   | 1     | MECF    | -34.04% |
|      |         | 2  | TRP   | 1.16%   |  | 2     | TRP     | -2.88%  |
|      |         | 3  | ELGS  | 2.01%   |  | 3     | COTE    | -2.48%  |
|      |         | 4  | SNG   | 3.16%   |  | 4     | TUFE    | -1.92%  |
|      |         | 5  | TGN   | 3.90%   |  | 5     | BIO     | -.89%   |
| 2016 | Highest | 1  | IARV  | 472.73% | Highest  | 1     | CNTE    | 131.47% |
|      |         | 2  | CNTE  | 131.47% |  | 2     | IARV    | 127.52% |
|      |         | 3  | ARS   | 82.42%  |  | 3     | PREB    | 36.67%  |
|      | Lowest  | 4  | PREB  | 53.22%  | 4  | BRM   | 32.70%  |         |
|      |         | 5  | MECF  | 46.71%  | 5  | ARS   | 23.99%  |         |
|      |         | 2  | TRP   | 1.02%   | 2  | RMAH  | -48.12% |         |



|      |         |   |      |        |         |   |      |          |
|------|---------|---|------|--------|---------|---|------|----------|
|      |         | 3 | IMP  | 2.30%  |         | 3 | ALR  | -40.97%  |
|      |         | 4 | TGN  | 3.26%  |         | 4 | SNP  | -34.91%  |
|      |         | 5 | SCD  | 3.87%  |         | 5 | CMF  | -14.46%  |
| 2017 | Highest | 1 | IARV | 60.05% | Highest | 1 | BRM  | 56.86%   |
|      |         | 2 | BRM  | 56.86% |         | 2 | IARV | 33.89%   |
|      |         | 3 | ARS  | 51.54% |         | 3 | ELGS | 21.15%   |
|      |         | 4 | OIL  | 45.20% |         | 4 | SNN  | 11.30%   |
|      |         | 5 | TBM  | 26.10% |         | 5 | ALR  | 8.03%    |
|      | Lowest  | 1 | TRP  | 0.61%  | Lowest  | 1 | OIL  | -178.10% |
|      |         | 2 | VNC  | 0.63%  |         | 2 | SNP  | -24.62%  |
|      |         | 3 | SOCP | 1.81%  |         | 3 | TRP  | -14.88%  |
|      |         | 4 | CBC  | 2.41%  |         | 4 | CMF  | -7.23%   |
|      |         | 5 | PTR  | 2.91%  |         | 5 | ATB  | -7.04%   |

Source: Author's own processing using SPSS 23.00

We further consider the fact that the use of provisions requires on the one hand, their recognition, which implies an expenditure recognition, and on the other hand their use, which implies the recognition of a revenue. Thus, we conducted a second series of adjustments in order to exclude both expenses and revenue reported for provisions from the earnings per share quantum.

From the data in Panel B (presented in Table 2) it can be seen that, on average, the exclusion of both expenses and revenues reported for provisions also leads to a positive change in dividends for many of the analysed cases, although significantly smaller than in the first case. Also, from Panel B presented in table no. 3 we can observe that in many of the analysed cases eliminating both the expenses and revenues reported for provisions may lead in fact to less distributed earnings (smaller dividends) than if they were recognized. This observation can be attributed to the fact that an undeclared and unrecognized risk may adversely affect the company, the loss being felt more strongly by the shareholders than when the provisions are recognized.

## 6. Conclusions

This paper had as a main purpose to identify if the use of provisions in accounting is able to produce significant changes in the amount of the distributed earnings (dividends) for the Romanian listed companies considering for that manner the paid dividends (according to [www.bvb.ro](http://www.bvb.ro)) and the corrected ones obtained after the exclusion of the expenses and revenues reported for provisions, under the mark of conservatism, from the earnings per share amount. The results indicate significant differences between the dividends actually paid and the potential dividends obtained by excluding the effects of the provisions recognition.

First, the exclusion of expenses reported for provisions leads to a *positive* change in the amount of the dividends for all of the analysed cases. Thus, if we were to consider only the exclusion of the expenses without addressing the corresponding revenues, due to the decrease or use of the provisions, we could argue that the situation of non-recognition of the provisioning expenses is a potentially favourable one for the shareholders who could be remunerated with more than if they are actually paid.

Second, considering the fact that the use of provisions requires on the one hand, their recognition, which implies an expenditure recognition, and on the other hand their use, which implies the recognition of a revenue we observed that, on average, the exclusion of both expenses and revenues reported for provisions also leads to a *positive* change in the amount of the dividends for many of the analysed cases, although significantly smaller than in the first case. Still eliminating both the expenses and revenues reported for provisions may lead in fact, in some cases, to less distributed earnings (smaller dividends) than if they were recognized. This observation can be attributed to the fact that an undeclared and unrecognized risk may adversely affect the company, the loss being felt more strongly by the shareholders than when the provisions are recognized.

Considering the abovementioned we can argue that the use of **provisions** under the mark of accounting conservatism in order to avoid decapitalization is a real fact for the company even though the investors seem to be placed on a second place. Moreover, despite the fact that it reduces the amount of distributed dividends, we can assert that their recognition benefits shareholders by minimizing the impact of losses from negative events.

## 7. References

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