

## **CONCEPTUAL DELIMITATIONS AND REGULATION ON THE PROFESSIONAL JUDGMENT IN ACCOUNTING**

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### ***Abstract:***

*The present article addresses the professional judgment both conceptually and in terms of regulations. Philosophical approach of reasoning has been justified since Antiquity and the literature reviews help conceptualizing professional judgment. The article highlights the situations in which the main national and international regulations in the field of accounting recommend the exercise of professional judgment. At the same time, they specify the frequency of both implicit and explicit references to the professional judgment concept in the regulations issued by the supervisory institutions of the accounting profession. In the last part of this paper we summarize some essential aspects regarding the judgment of the accounting expert and of the financial auditor, too.*

**Key words:** *professional judgment, national regulations, international regulations, accounting profession.*

**JEL Classification:** *M41*

### **1. Judgment – the concept of the philosophical vision**

In the quest for knowledge, a number of philosophers have been preoccupied with judgment, thus contributing to the development of the spectrum of judgment.

David Ross brings us to the forefront the Aristotelian vision on reasoning, which has been lifted to the absolute rank by the philosopher of Ancient Greece. Aristotle states that reason is represented as the most authoritative element within human beings, what they themselves truly are; what it is that gives satisfaction to humans. Aristotle also divides reason into two elements: passive and active reason. With regards to passive reason,

we find out that it represents the act of understanding, while active reasoning enables passive reasoning to move from the potential of knowledge to the present of knowledge [Ross, 1998]. Reason is the most systematic thing in the world, which amplifies and establishes the primordial place occupied by reason at the level of the entire existence [Descartes, 1990].

From a Kantian perspective, reason is the main source of formation of knowledge principles a priori [Kant, 2009], while in the Paschal philosophical vision [Lazăr, 1991], reason is not inscribed in the very being of the man: it is the ultimate determination of its value.

## **2. The Methodology of Research**

The main objective of our material is to highlight the importance of the professional judgment in the accounting profession. In order to achieve the objective, we have tried to conceptualize the notions of "judgment" and "professional judgment" using as a research method the study of specialized literature and of the legislation in the field regarding the "professional judgment" when it comes to the accounting profession. As a result of information centralization, we have applied as a research method the synthesis, thus we have pointed out some situations when the exercise of professional judgment is recommended.

## **3. Conceptual development of the expression "professional judgment"**

The conceptualization of the term of professional judgment puts us in front of a collocation difficult to solve, which is addressed in the multi-professional environment.

In generic terms, reason is that logical chain of judgments which lead to a series of arguments and findings [www.dexonline.ro], and the notion of professional judgment implies applying the knowledge and the experience gained as a result of relevant training relevant [Ivan, 2016].

Professional judgment is that concept which is to be found, to a larger or smaller extent, in the application of accrual accountability as well as in the assessment of the continuity of the activity, thus the proper application of the accounting regulations for the purpose of exact representation of the economic situation falls under the responsibility of the account expert. The use of professional judgment in the accounting area, in a consistent manner, is considered to be primary, thus eliminating the possibilities to reach erroneous conclusions [Feleagă și Feleagă, 2007]. Professional judgment is considered a cornerstone of the accounting profession since the true image depends on the way it is utilized and the accuracy with which it is exercised [Cuzdriorean, 2013]. The application of a professional judgment based on well-defined principles provides the auditors the opportunity to thoroughly apply their experience, their acquired knowledge, while preventing work

running due to the existence of strict rules will only lead to the limitation of a diverse approach [Span, 2012].

#### **4. Regulatory delimitations on the current state of knowledge and the use of professional judgment in the accounting field**

Both at national and international levels, the field of accounting is regularized and within these regulations the exercise of professional reasoning is invoked, too. In the regulations issued by the Ministry of Public Finance [O.M.F.P. 1802/2014], **professional judgment** is approached about in:

- the determination of certain immobilizations which may contain both tangible and intangible immobilizations, using reasoning to decide which element is more significant;
- evaluating the degree of safety with regards to future economic benefits;
- recognizing a tangible immobilization;
- determining whether a real estate property is a real estate investment or not;
- exercising joint control.

International Financial Report Standards (IFRS) corroborated with International Accounting Standards (IAS) mention professional judgment both implicitly and explicitly in the regulations listed in table no. 4.1. [www.ifac.org].

Table. no. 4.1. Mentions of professional judgment in IFRS/IAS

<b>IFRS/IAS</b>	<b>Mentions regarding professional judgment</b>
IAS 1 <i>Presentation of financial statements</i>	mentions <b>professional judgment</b> ten times in determining the way of presenting the Annual Financial Statements, in the process of applying the accounting policies, in the assets recognition, in the choice for the depreciation method, in establishing the threshold of significance, in estimating the results and the financial statements.
IAS 16 <i>Tangible immobilizations</i>	mention <b>professional judgment</b> in determining the elements of tangible immobilizations;
IAS 29 <i>Financial reporting in hyperinflationary economies</i>	encourages <b>professional judgment</b> in order to reshape financial statements;
IAS36 <i>Assets depreciation</i>	encourages the application of <b>professional judgment</b> in the determination of cash-generating units;
IAS 40 <i>Real estate</i>	mention the <b>professional judgment</b> in order to

<i>investments</i>	determine whether a real estate property can be a real estate investment;
<i>IFRS 7 Financial instruments: disclosures</i>	mention <b>professional judgment</b> both in determining the fair value and the accounting value within the financial assets and financial liabilities, as well as in determining risk concentrations in financial instruments;
<i>IFRS 9 Financial instruments/ IAS 39 Financial instruments – recognition and measurement</i>	mention <b>professional judgment</b> in order to estimate the value of the depreciation loss and also to adjust the data so as a group of financial assets reflect current situations;
<i>IFRS 11 Joint ventures</i>	mention <b>professional judgment</b> in order to establish whether a joint commitment is a joint exploitation or a joint association;

### 5. Judgment in the accounting profession

The accounting profession is defined as the ensemble of activities which involve vast accounting knowledge, of the professionals who carry out these activities as well as of the professional bodies [Toma și Potdevin, 2008]

The necessity of the occurrence and the exercise of professional judgment in the accounting profession is due to the situations in which the regulations in the field or any other indications are not enough to solve the cases that any specialist has to face, thus appealing to professional judgment is encouraged.

Whereas the accounting profession is given the responsibility to protect the public interest, this has called for the necessity of some national and international professional bodies designed to regulate and supervise the professionals' activity. Thus, whether we talk about the institutions which regulate and supervise the activity of the accounting expert, such as the International Federation of Accounting or the Chartered Accountants Board and of the Certified Accountants in Romania (CECCAR), whether we talk about the institution supervising the auditor's activity and this is the Chamber of Financial Auditors in Romania (CAFR) or we talk about the institution to regulate and oversee the activity of the tax consultant, that is the Chamber of Tax Consultants in Romania (CCFR), the concern for the exercise of professional judgment is unanimous.

When drawing table no. 5.1., we have used the implicit and explicit counting of the expression "professional judgment". Thus, after analyzing the data from the table, we have realized that the total number of the professional judgment term, both at national and international levels, is of at

least 272 times, which is a significant number, at the same time we have noticed that professional judgment has been mentioned the most in the International Audit Standards, and that is due to the diverse nature of the audit missions.

**Table no. 5.1. Mentions of the professional judgment under the regulations of the accounting profession supervisory institutions**

<b>National and international regulations</b>	<b>Number of “professional judgment” entries</b>
<b>Board of Chartered Accountants and of Certified Accountants from Romania (CECCAR):</b> -National Code of Ethics for Professional Accountants, CECCAR Publishing House, Bucharest, 2011.	13
<b>International Ethics Standards Board for Accountants (IESBA):</b> -Code of Ethics for Professional Accountants.	28
<b>International Accounting Standards Board (IASB):</b> International Financial Reporting Standards /International Accounting Standards.	28
<b>Romanian Chamber of Financial Auditors (CAFR):</b> -Act number 73/2006 from 20 /09/2006, published in the Official Gazette, Part I, No, 909 from 08/11/2006 on the approval procedures for the quality control of the financial auditor activity and related services; -The Norm from 19/01/2005 – updated version on 08/08/2007 regarding the period of practical professional training of the trainees in financial audits; -The Norm from 26/08/2011 published in the Official Gazette, Part I, No. 715 from 11/10/2011 regarding the tax expertise at the request of Courts, of criminal investigation bodies, of tax bodies or of other interested parties.	9
<b>International Federation of Accountants (IFAC):</b> International Standard on Auditing ISA.	186
<b>Romanian Chamber of Tax Consultants (CCFR):</b> -The Norm from 26/08/2011 published in the Official Gazette, Part I, No. 715 from 11/10/2011 regarding the tax expertise at the request of Courts, of criminal investigation bodies, of tax bodies or of other interested parties; - The Annex from 30/07/2007 published in the Official Gazette, Part I, No. 647 from 21/09/2007, encompassing the Code on ethical and professional conduct in the field of tax consulting.	8

Since the accounting profession collects more liberal professions, we shall approach several aspects regarding the judgment of the accounting expert and of the financial auditor. The accounting expert presents an important role in society and therefore it is necessary that he obeys the following basic principles [Toma și Potdevin, 2008]:

- integrity – to be honest and truthful in the activity carried out;

- objectiveness – to be impartial and to not allow the conflicts of interests or preconceptions to interfere with the professional activity;
- professional competence and prudence – to maintain the optimal level of knowledge and at the same time to act prudently;
- confidentiality – to respect confidentiality of the information acquired in the exercise of professional competence;
- professional behavior – to comply with the legislation and the relevant norms of the profession so as not to discredit the profession;
- respect towards technical and professional norms – to carry out the responsibilities and duties of the profession without ignoring the technical and professional standards;
- independence – implies the exercise of the profession in an objective and fair manner.

As you could notice, whether we talk about the application of national rules in maintaining and organizing accountancy or we talk about the compliance of the International Standards of Financial Reporting or of the International Standards on Accounting, it is desirable that the chartered accountant should exercise his professional reasoning.

For example, the exercise of professional judgment is required when purchasing a complex asset, where there are both buildings and land. Whereas the parts of an asset have a different life span, the chartered accountant will proceed to the separation of the two elements of the asset and implicitly to the depreciation of the buildings, the land not being depreciable as it is considered that its useful life is unlimited. At the same time, when recognizing immobilizations we can take as a good example of exercising the professional judgment the situation when the chartered accountant considers as adequate the aggregation of some elements which, if they were taken individually, they would be insignificant, such as the molds, the measuring and control tools or the like and which apply the criteria for recognizing their aggregate value.

It's also in immobilizations when, in order to establish whether a permanent capital, which incorporates both tangible and intangible assets, should be treated as tangible or intangible immobilizations, it is necessary to use judgment so as to assess which element is more significant than the other. To determine whether a real estate constitutes a real estate investment or not, we need professional judgment. Entities should develop criteria so as to exercise their professional judgment in a consistent manner, in accordance with the definition of the real estate investment.

The most important moment in using professional judgment may be the evaluation process. Evaluation involves judgments based on the latest credible information available. This has to be reviewed when the

circumstances change or as a result of new pieces of information or of a better experience.

Whether we refer to the financial or the internal auditor, the role of the professionals, controlled at national level by the Chamber of Auditors in Romania, is to verify and certify a real and complete reflection in accounting of the financial statements and of their true image; the ultimate goal is that to increase the degree of confidence of the users of the financial statements audited [Popa, Mihăilescu, Șpan și Stănescu, 2012]. The International Standards on Auditing [www.ifac.org], as main regulations in exercising the audit profession, mention the professional judgment both implicitly and explicitly in the regulations listed in table 5.2.

**Table no. 5.2. Mentions of professional judgment in the International Standards on Auditing (ISA)**

ISA	Mentions of professional judgment
ISA 200 The general objectives of the independent auditor and the development of an audit in accordance with the International Standards on Auditing	require the auditors to keep their <b>professional judgment</b> during the planning and deployment of an audit mission;
ISA 300 Planning of an audit on financial statements	invokes the use of <b>professional judgment</b> in establishing the threshold of significance and the test of the significance threshold as well as its interpretation.
ISA 315 Identification and assessment of the risks of distortion by understanding the entity and its environment	implies the exercise of <b>the professional judgment</b> in understanding the economic entity and its environment.
ISA 700 Forming an opinion and reporting on financial statements	invoke <b>professional judgment</b> in order to form an opinion on the audited financial reporting.

The repeated reference of the notion of professional judgment within the International Standards on Auditing reflects the importance granted to the exercise of reasoning in the audit missions and, at the same time, the particular situations that the financial auditor faces when exercising his/her profession.

## 6. Conclusions

Reason has been studied ever since before our Era, which can only confirm the importance of this notion, and the pedestal on which it has been situated by the great philosophers and thinkers of the world urges us to pay particular attention to judgment.

During the elaboration of this paper, we have ascertained the conceptualization of professional judgment in the specialized literature, which demonstrates us the increasingly stronger concerns with respect to this concept and, at the same time, shows us the importance of professional judgment, a “cornerstone” of the accounting profession.

The science of accountancy is no longer precise because the provision of information from the annual financial statements to help the decision-makers implies resorting to the professional judgment in accounting. The problem of professional judgment has an interdisciplinary character and it is met in various fields of activity, such as in Medicine, Law, Psychology, Accountancy etc. In the present study we have referred to the problem of professional judgment in the field of accounting. Professional judgment is a concept that the IFRS norms “deal with”. Taking into account the harmonization of the Romanian accounting system with the international accounting standard, this concept has been taken over by the national regulations in the field.

It has been found that due to the important role that is played by the exercise of the accounting profession, namely that of protecting public interest, this has been regulated and supervised by institutions both at national and international levels. Thus, in the course of this paper, I have managed to ascertain the large number of implicit and explicit mentions of the concept of professional judgment that derive from ethical codes, from international standards and from the norms elaborated by the regulatory and supervisory institutions of the accounting profession. The fact that the expression of professional judgment has been approached in a significant number reveals the importance of the exercise of professional judgment, whether we refer to the accounting expert, to the tax analyst, to the auditor or to other accounting professions.

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