WINNING THE BATTLE OF ETHICS

An Honors Thesis (ID 499)

by

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OVERVIEW

This thesis attempts, first, to lay a framework for the broad discussion of ethics by discussing the three general ways to approach ethics, and why ethics are important to professions, particularly the public accounting profession. The thesis explores two reasons for increased ethical concerns, one is specific to the accounting profession and one is universal. It examines actions currently being taken by public accountants to deal with the increased concern, and, finally, addresses potential actions that can be done in the future to enhance the ethical conditions of public accounting.

INTRODUCTION

A code of ethics is a system of conduct based on moral duties or obligations that indicates how we should behave. Basically, what is considered ethical is a matter of social judgement. It differs from culture to culture and person to person. There are three general ways to approach an ethical problem. Joseph Fletcher (1978) calls these three ways the legalism, antinomianism, and situations approaches. Legalism is the approach where one enters into every decision making situation encumbered with the whole apparatus of prefabricated rules and regulations; emotions are not allowed to interfere with "justice." The antinomianism approach is the other extreme in which there are no principles, rules or maxims. The situation is expected to provide the ethical solution; there is
no logic in this approach. The situation ethic approach uses reason as the instrument of moral judgement. There is a knowledge and respect for the rules and principles, coupled with the realization that circumstances alter the case. The emphasis is on the legal dictum, "what is reasonable in any particular case must depend on the facts of the case." I think the situation ethic approach is the preferable one and should be the basis for the professional code of ethics.

A profession’s code of ethics is one characteristic that distinguishes it from a vocation. A profession’s code of ethics is a set of rules and percepts designed to induce an attitude and a kind of behavior on the part of the practitioner of the profession concerned, which will encourage public confidence. A code of ethics is necessary in professions possessing a responsibility to the public, a complex body of knowledge and a need for public confidence. Because the general public usually doesn’t have the knowledge needed to evaluate the correctness of the practitioner’s advice or actions; the public must depend on the code of ethics to ensure the practitioner exerts his/her efforts for their betterment.

Many professionals believe that as long as their conduct meets current standards of practice, little more can be asked of them. However, Robert A. Cooke (1988) states laws and regulations are reactive and slow to change; ethics should be proactive, and attempt to anticipate problems. R. K. Maultz and Hussein A. Sharaf (1978) quoted John Locke as stating, "Truth,
ethical conduct, and moral principles are not innate. They can only be acquired through perception and conception." A professions code of ethics needs to involve more positive action. If it doesn't an expectation gap may occur between what a professional is doing and what the public believes he is doing. Unresolved expectation gaps undermine a professions attempts to appear ethical and lead to serious threats to a professions survival which is dependent on the public's confidence in them.

Professionals have responsibilities to their clients, societies, other members of their profession and themselves. All responsibilities must be considered when drawing up a code of ethics. Anytime one or more of these responsibilities get neglected or out of balance, the professional has failed to discharge appropriate professional responsibilities. John L. Carey (1978) states public accounting calls for the "cultivation of the sense of objectivity to an extraordinary degree, a judicial detachment, and an unassailable integrity in addition to wide professional knowledge and high technical skill."

A major part of public accounting, the attestation service, consists of providing assurance that the information the public is relying on is accurate and fair; thus, assisting the public in making decisions based on the information. However, in the words of Carey (1978):

The opinion of a certified public accountant on a financial statement is of value only so long as those who read it believe that it is the
opinion of an independent, disinterested, impartial
expert who is uninfluenced by anything but the
desire to tell the truth, the whole truth and
nothing but the truth.

Carey also notes that relationships shift very rapidly in the
business world. If the accountant tries assiduously to reduce a
tax bill for a client, the client, when seeing the accountants
signature on an audit report, may wonder if the accountant
applied similar zeal in the interest of management. For the
public that believes in the "don't bite the hand that feeds you"
mentality, it can be hard to believe that public accountants
will risk losing clients that pay their fees by insisting on
complete compliance. Cooke (1988) states "The standard joke is
that business ethics is a contradiction in terms in the same way
military intelligence is." The increase in variety of services
offered by public accounting firms and the current business
environment is causing many to reconsider their assessment of
the state of ethics in the public accounting profession.

PROBLEMS

Public accounting has expanded from tax and auditing
services to many diverse attestation, management advisory, and
litigation support services. This expansion creates image
problems for public accounting. By expanding into services,
such as litigation support, where there are no set standards,
the accountant opens himself to ethical problems. He must
choose which general standards to apply and how. This liberty may result in misinterpretations or the stretching of rules from other areas to fit situations where they don’t really apply.

Cooke (1988) believes that many cases of impropriety originate in environments where lines of accountability are vague or nonexistent. Conflicting standards may also result in dilemmas. John W. Buckley (1978) believes that one of the most serious challenges facing the public accounting field today is that the variety of services offered is causing alterations in client identity. In attestation service, the actual client is the public. The company paying the fees needs the public accountant’s credibility to "sell" its information to the public. Without an independent audit, the public has no assurance that the company is telling the truth about its financial standings. Without the assurance, decisions such as investing or granting credit takes on an undesirably high level of risk. With services such as management advisory and litigation service, the client identity is shifting to the private company. Also, these services cause the public accountant to work with the companies in a nonindependent status. This can create the question, "Is the accountant a servant of the private industries?"

Buckley (1978) believes that some prominent members of the public are beginning to raise the question "Is the accounting profession maximizing the private good of the company rather than the public good of society?" If the same company uses the
firm's tax, auditing, management advisory, and litigation service thereby creating substantial revenue for the firm, can the auditor risk losing the client to another firm? These questions become even more pressing when looked at in the context of the growing environmental concerns.

Many feel that the business environment is creating ethical problems. Robert Frank (1989) contends:

Contrary to Adam Smith's clear intention, his invisible hand planted the idea that moral behavior might not be necessary, that the best of all possible worlds might result if people were to simply pursue their own interests. Darwin's survival of the fittest went a step farther creating the impression that failure to pursue self interest might even be hazardous to our health. Smith's carrot and Darwin's stick have by now rendered character development an all but completely forgotten theme in many industrialized countries...

Opportunistic people feel their actions don't affect the world; therefore, they take whatever they want and expect others to do the same.

As more and more people begin to take think like the opportunistic people, it becomes difficult for even those that are basically honest to continue to do what is honest even if it is detrimental to them in someway. Someone who expects always to be cheated has little motive to behave honestly. K.A. Merchant, as quoted by Ahmed Belkaoui (1989), said:
By providing incentives for deception, by failing to persuade managers and employees that chances of detection are high and penalties severe, and by failing to provide adequate moral guidance and leadership, corporations increase the use of illegal and unethical practice.

Frank (1989) found economic and business students were most likely to behave opportunistically. Thomas Piper, associate dean of Harvard Business School, was quoted by Paul Wilkes (1989) as saying:

"We were so concerned with economic self-interest, so enamored of exciting new concepts - for instance, Japan's just-in-time delivery. Maybe we were hoping for just-in-time values."

Frank (1989) believes that the moral teaching is failing for three reasons. First, is the decline in religion with no substitute institution to take over. Also, there is an increase in dual-job and/or single-parent families that are unable to devote the necessary time and energy to the task of teaching morals. Finally, ethics are not taught in schools due to respect for diversity of beliefs.

Kenneth Blanchard (1988) has observed, "Competition has fostered a "get the buck and get out" mentality that causes us to operate out of fear. No field, profession, or industry, it seems, has gone untouched by some scandal or another."

A survey appearing in U.S. News and World Report in 1988
stated that seventy-six percent of 1,082 respondents said they thought decaying cultural and social institutions were the main factor in the erosion of business ethics. Other factors that were frequently mentioned as reasons for the erosion of business ethics are increased concentration on short term earnings, doing business in cultures with different ethics, and volatile economic conditions. Forty-eight percent of the respondents said they thought professional guidelines and accreditation was the reason for ethics among professionals. Others credited peer opinion and approval, education and socioeconomic backgrounds for ethics among professionals.

A survey done by Personnel Journal indicates that the main factors contributing to a breach in ethics is a desire to "make it" before it's too late, and a belief that "the end justifies the means" according to Blanchard (1988).

SOLUTIONS

Due to pressure from the public and the government, the American Institute of Certified Public Accountants (AICPA) has taken steps to resolve ethical problems in public accountant.

In 1987, the AICPA restructured the Code of Ethics in hopes of reducing the expectation gap between what the accountants are doing and what the public believes the accountants are doing. Also, in the January 19, 1990 CPA Letter, it was reported that AICPA members, by a more then six to one margin, approved a measure that made it mandatory for any CPA firm that audits
clients registered with the Securities and Exchange Commission (SEC) to be a member of the AICPA’s SEC Practice Section. Membership in this section requires a firm to undergo peer reviews and be subject to public oversight. But, there is still much to do to enhance the public accountant’s image.

I think there needs to be a realisation of the two ethical models explained by Frank (1989). The first one is the traditional rationale model. The individual under this model is convinced that the penalties for being unethical are severe, the risk of getting caught is high, and it is necessary to be ethical to gain the trust of others. This model, however, doesn’t prevent unethical behavior in situations when the encounter between the persons are fleeting and/or others are not likely to observe or learn of the behavior.

As a result, I think there needs to be an emphasis on the second model, the commitment model. In this model, honesty is a character trait that is desirable and recognizable by others. In order to develop this character trait, the individual must indoctrinate and practice ethics. If the individual fails to act correctly, regardless of whether the behavior is observed, there is failure to maintain the predisposition to honesty. After doing wrong several times, it becomes difficult for the individual to perceive him/herself as being an ethical, honest person which, under this model, is top priority. Therefore, the individual has failed at sustaining the emotions that motivate honesty. Others will notice this change in the individual’s
emotional composition and, as a result, redefine their expectations and opinions of the individual. The model states that the individual needs to believe that the adverse effects of the shifting opinion of others and your own opinion of yourself is not worth any possible positive outcomes of being unethical.

I think it's important for the individual to analyze which model they are using and be aware of possible shortcomings of the traditional rationale model that may lead them to temptations to be unethical. Perhaps there should be an additional essay added to the principles section of the AICPA code of ethics discussing the difference and commending the commitment model.

Frank (1988) believes the moving force behind moral behavior lies not in rational analysis but in the emotions. Feelings of moral responsibility are much more focused on those with whom we have close personal ties. Large institutions are often "depersonalized"; therefore, no emotional feeling and/or moral responsibility is felt. I believe that the public accounting profession needs to become more personalized. I think there needs to be an emphasis on loyalty between the individuals within the profession. This loyalty and group identity can increase feelings of moral responsibility within the profession which ultimately will benefit the public. I think one way to do this is to mandate peer review. Not only does it facilitate interactions among those in the profession; but, it can assist
in making the accountants realize that what they do affects others.

Another way to achieve this goal is through education. I believe ethical education is important for many reasons. As Robert L. May (1989) points out, all individual members within the accounting field must be convinced that the code is more than a symbol. One way to accomplish this is through education. Carey (1978) believes that the remedy for ethical problems is a deeper understanding among accountants of the essential meaning of the rules, their background, and the purpose for which they were adopted. It has been proven in psychological studies (R.H. Fazio, 1986) that when individuals are in stressful situations in which they are highly aroused, it is harder for them to access their values, if those values don't "come readily to mind." According to Wilkes (1989), John Whitehead, ex-Deputy Secretary of the State and investment banker, said quick decisions are being made under extreme pressure every day. training in how to look at these decisions is very desirable. If ethic education is implemented and the accountant has thought through stands on ethical issues via case studies, he will be in a better position to respond to the situations in ethical ways. The focus on ethics earlier will make it easier for accountants to remember their values. And, as Mautz and Sharaf (1978) point out, knowledge of the ultimate outcome of his actions on himself and others, awareness of society's requirements, feelings of obligation, and recognition of the
norms of ethical conduct help professionals and individuals attain high degrees of ethical conduct. Blanchard (1988) says, we need to bring matters back down to basic levels with a focus on people.

I believe that ethics can and should be taught on a logical basis. For example, the Process Seven Reason Model practiced by Arthur Anderson & Company is a comprehensive method of dealing with ethical problems. The first step is to determine the facts of the situation. From the facts, there must be an inference of ethical issues. Based on the ethical issues identified, the individual should try to think of all the stakeholders, all of the people who will be affected by the decision. Then, the individual should brainstorm for alternatives. In this step, the focus should be on getting as many alternatives as possible and not on the quality of the alternatives. After thinking of as many alternatives as possible, the individual should analyze the alternatives by considering the ethics of each alternative (step five) and the practical constraints of the alternative (step six). I think in analyzing the alternatives, the individual should consider the three question ethic checklist developed by Blanchard (1988): is it legal, is it balanced (neither party gets unfair advantage), and how will it make me feel about myself? Gene R. Lacziak (1983) offers five alternative ethical standards. The first is the golden rule standard, it says the individual should act the way they would expect others to act towards them. The utilitarian principle
suggests individuals should act in a way that results in the
greatest good for the greatest number of people. Kant’s
categorical imperative model says that individuals should act in
a way that the action they take could be a universal law or rule
of behavior under the circumstances. The fourth model, entitled
the professional ethic model, suggests the action taken should
be the one a disinterested panel of professional colleagues
would view as proper. The final model is the T.V. test. The
individual should only do behaviors that they would feel
comfortable explaining the reasons for the action to a national
television audience, which is assumed to be composed of honest
people from whom the individual wants approval. Cooke (1988)
adds a sixth standard called the enlightened self-interest
model. This model says each individual should maximize net
benefits for himself in a way that minimizes harm to others,
when possible. Finally, step seven involves deciding which
action to take and following it through.

Ethical teaching should also emphasis the five principles of
ethical power brought out by Blanchard (1988). The first of
these is purpose. There should be ongoing guidelines that, by
design, can never be achieved. Secondly, there needs to be
pride or good self-esteem which will assist the individual in
standing up for what he believes in. However, an extreme ego
might foster the belief that “I am above the rules” or other
such temptations to be unethical because, “I deserve this.” The
individual should be a patient person as impatience spawns
temptation to cut corners which can result in unethical behavior. The individual needs to be persistent. They can’t give up in the face of opposition and take the easy (often unethical) way out. Finally, the individual must keep their sense of perspective. They should avoid the “ready, aim, fire” philosophy that can cause a person to lose sight of their purpose. The emphasis should be on long-term, not short term, goals. An individual stands a much better chance of being able to solve ethical problems in the best possible manner by developing the five principles of ethical power: purpose, pride, patience, persistence, and perspective.

Martin Barradell (1978) states, “The standing, if not the very existence, of a profession depends on the continuance of public confidence in the standards of its members...” If the public accounting field wishes to survive and prosper, it cannot ignore the ethical problems prevalent in our society today. As Mautz and Sharaf (1978) maintain, individuals may assent to several moral rules and be convinced of their moral obligations by education, customs common to their country, or any number of other ways, but, however persuaded, these moral rules become the individual’s conscience. The public accountant field needs to ensure that its members have a conscious. In Carey’s (1978) words:

“No one should enter the public accounting practice without having a clear idea of just how far he is willing to go in satisfying each client, to what
extent he may subordinate his personal preference, just how much he can compromise, and exactly at what point he is determined to refuse to go farther with a polite statement of the reason."
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