

ACCOUNTING TRANSACTION ETHICAL EVALUATIONS

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ABSTRACT

This exploratory study reports the findings of an investigation aimed at assessing differences in ethical evaluations made by accounting practitioners (CPAs) and students studying to become CPAs in East Texas. The investigation used modified managerial and accounting recognition scenarios used in previous studies (Merchant and Rockness 1994; Grasso et al. 2009). In addition to determining decision making tendencies, demographic variables such as age, work experience and academic credentials were investigated. Significant differences were discovered as the student evaluated the operating and accounting decisions as more unethical than did the accounting professionals.

Keywords: Ethical evaluations, Students, Accounting Professionals, and East Texas

BACKGROUND

During the past decade, corporate scandals, fraud, and financial report restatements have been persistent in the news headlines. Critics of the accounting profession claim that these events are the product of poor professional judgment, especially poor ethics. Lam and Samson (2005) report cleverness and creativity have replaced the traditional honesty and integrity which characterized accountants of the past.

ETHIC AWARENESS

Accounting educators have responded to the claim for more ethical awareness by modifying curriculum to cover ethical studies and training (Bernardi and Bean 2006; Haas 2005). Professional Accounting Boards have also responded to the need to modify accounting curriculum. The Texas State Board of Public Accountancy's (TSBPA) Behavioral Enforcement Committee received lots of complaints against CPAs who did not understand the Rules of Professional Conduct. In January 1995, Texas initiated the ethics continuing professional education (CPE) requirement (TSBPA 1994) which requires each licensee to complete a two-hour mandatory ethics CPE course every three years. The ethics requirement changed again in January 2005 to a four hour biennial mandatory ethics CPE update (TSBPA 2004).

Place in the Academy

The TSBPA requested Texas colleges and universities to include a state board approved ethics course in their curriculum effective July 2005. The requested ethics course attempts to raise the level of ethical reasoning utilized in public accounting and became a requirement for those applying to sit for the CPA exam in Texas. According to Barbara Stooksberry (personal correspondence to authors, March 4, 2011), TSBPA Publications Editor, “forty-five Texas schools had ethics courses in place for the fall semester of 2004 so that their students would be able to meet the 2005 ethics requirement.” Stephen F. Austin State University (SFASU) began offering a required discrete accounting ethics course that met the TSBPA criteria in the fall semester of 2004. The University of Texas at Tyler (UTT) also began offering a general business ethics course in the fall 2004 semester. The UTT class met the TSBPA criteria but was not required: instead it was highly recommended for accounting majors.

Several studies focus on whether students’ moral and ethical reasoning can be positively influenced by a discrete course in accounting ethics (Dellaportas 2006; Welton et al. 1994; Armstrong 1993; Thompson et al. 1992; Lampe 1996). According to researcher Rest (1986), additional education is an important factor to increase the development of moral reasoning. That ethics education matters is well supported in the literature (Dellaportas 2006; Welton et al. 1994; Armstrong 1993; Thompson, et. al. 1992; Lampe 1996). In addition, Lau (2010) reports that ethics education improved students’ ethic awareness and moral reasoning. The members of the American Institute of Certified Public Accountants are also subject to its ethics rules (Mintz and Morris 2008, 102). According to Aghimien and Fred (2010) over half of the states require candidates that successfully pass the CPA exam to complete and pass an ethics exam prior to obtaining a CPA license or certificate.

Prior to 2000, business ethics had a low profile. During the early 2000s given SOX, Enron, WorldCom, Arkadelphia, Tyco, Xerox, Health South, and other exposed events, business ethics was in the limelight and a very high concern. Currently, the concern and emphasis on ethics is relaxing somewhat (Magnet 2011). The recent problems with mortgage companies and financial institutions remind educators that accounting programs still need to emphasize ethical conduct and behavior.

THE STUDY

This study focuses on the evaluation of accounting transactions of accounting professionals and those who aspire to become accounting professionals in East Texas. With the TSBPA adoption of required continuing ethic CPE training for Texas accounting professionals and required academic ethics course for students who aspire to sit for the CPA exam in Texas, this study investigates if difference exists in the ethical evaluation of accounting transactions between the East Texas TSCPA members and students.

This investigation is restricted to those accounting professionals (N=803) practicing in the East Texas region serviced by the East Texas Chapter of the Texas Society of Certified Public Accountants (ETCTSCPA). The East Texas Chapter is the sixth largest TSCPA chapter in Texas and its members represent 20 counties in North Eastern Texas. As displayed in Exhibit 1, the East Texas TSCPA members have held their CPA certificate for a longer period than their state-wide colleagues, fewer work in industry, they tend to be female, and are somewhat older than their state-wide associates.

The students in the investigation (N= 612) are studying to become accounting professionals at the two four-year higher education institutions that offer the TSBPA criteria that meets all requirements to take the CPA exam in Texas - SFASU and UTT. The students are classified as juniors, seniors and master program students that have elected to study the curriculum necessary to sit for the CPA exam. The use of human subjects in the investigation complies with applicable university policies at both SFASU and UTT.

Data was collected through the use of a modified questionnaire developed by Merchant (1989) and used by other researchers (Burns and Merchant 1990; Merchant and Rockness 1994; Grasso et al. 2009). The questionnaire consists of 13 short scenarios that describe possible questionable operations or accounting management decisions at a hypothetical manufacturing firm. The financial data in the scenarios were amended using the Consumer Price Index to change amounts from their original 1989 values to comparable 2010 values (US Department of Labor 2011).

The study participants are asked to evaluate each scenario by indicating their judgment as to the ethical nature of the transaction using the following scale: 1 = ethical decision, 2 = questionable decision, 3 = moderately unethical decision, 4 = seriously unethical decision, and 5 = totally unethical decision. The scenarios are designed to respond to operating decisions or to an accounting decision that would normally be part of an audit review (Exhibit 2). Scenarios 1, 2, 3, 5, 6 and 7 address management operating decisions whereas the remaining scenarios address accounting decisions.

DATA COLLECTION

Survey Monkey was used to email the questionnaire to the study participants. Only 700 valid email addresses were available for the practitioners. Of the questionnaires sent to the accounting professionals, 225 were returned for a 32.14 percent response rate. Of the 612 emailed to students, 133 were returned for a 21.7 percent response rate. Each of the response rates is consistent with social science survey results (Kaplowitz et al. 2004). The responses from both accounting professionals and students were divided into early and late responders. Analysis found no significant differences between the two groups of responders suggesting that nonresponse bias did not impact the results.

FINDINGS

In general, prior studies found the managerial decision scenarios to be ethical (Merchant and Rockness 1994; Grasso et al. 2009). The same studies found the accounting decision scenarios to be unethical. This study disagreed with the Merchant and Rockness (1994) and Grasso et al. (2009) studies regarding the level of unethical managerial decisions but agreed with their findings concerning the accounting recognition decisions.

Types of Accounting Transactions

The thirteen different accounting transactions were analyzed utilizing a Principle Components Analysis with rotation using SPSS Version. Prior to performing the analysis, the suitability of the data for factor analysis was assessed. Inspection of the correlation matrix revealed the presence of many coefficients of .3 and above. The Kaiser-Meyer-Orkin value was .64 (Kaiser 1974; Tabachnick and Fidell 2007). The Bartlett's Test of Sphericity (Bartlett 1954) obtained a Chi-Square of 1364.4 with df 78 and significant at .000 which supports the factorability of the correlation matrix.

The analysis revealed the presence of two components with Eigenvalues greater than one. An inspection of the screenplot revealed a clear break after the second component. Table 1 displays the rotated factor matrix. The two factors explain 41.45 percent of the variance of the 13 transactions. All of the large coefficients are positive, indicating the factors have the same directionality as the original value, i.e., large values indicate an unethical rating and small values indicate an ethical rating.

The first factors appear to represent dimensions discussed by Burns and Merchant (1990) as accounting manipulations. The seven accounting scenarios loaded on the first factor that involves accounting recognition and reporting. This factor explains 22.61 percent of the variance of the 13 transactions. The second factor is operating management transactions as they clearly manipulate activities as directed by the chief operating/management officer. This factor explains only 18.84 percent of the variance of the 13 transactions.

Prior to analyzing the differences among groups of respondents, the means of the 13 scenarios grouped by the factors on which they loaded was examined. Table 2 displays the mean responses to these original scenarios and the mean of the scenarios and the mean for the each factor. Earlier studies find (Burns and Merchant 1990; Grasso et al. 2009) that manipulating accounting methods is less acceptable ethically than manipulating managerial decisions. This analysis supports that finding as the scenarios within accounting manipulation factor has an overall means of 3.97 that indicates that the scenarios were considered most unethical. In the accounting manipulation area, there was little difference between the respondents' rating of the unethical acceptability of manipulation by means of adjusting inventory valuations and other forms of accounting manipulations. Within the managerial operating scenarios, the respondents felt the manipulations that changed the timing of expense recognition were much more questionable ethically than manipulations which changed revenue timing. However, the

scenarios within the managerial factor have an overall mean of 2.15 that indicates they were less unethical than the accounting manipulations.

Practitioner versus Student Ethical Evaluations

Table 3 displays the comparison for each scenario of the reported professional ethical acceptability compared to the student ethical acceptability. No significant difference was found among the levels of ethical acceptability value between the student and practitioner groups for the accounting recognition scenarios. These include Scenario 4 recording supply cost next year, Scenario 9 writing down inventory value, and Scenario 11 writing up inventory value to reach profit target. The two groups' ethical acceptability values significantly differed on all other scenarios that include both managerial and accounting recognition decisions with students displaying a much more idealist decision of unethical acceptability. This supports Valentine and Bateman's (2011) study that used students to investigate ethical reasoning in different business situations. They found (p 162) students scoring high on idealism and relativism measures. Practitioners' experience with the effect of valuation changes on accounting numbers may condition them to the unethical acceptability of this practice. Students, however, have little or no experience with valuation change opportunities and are a bit more idealistic. Given these findings, when students are compared to professions, it is reasonable to find students identifying situations to be more unethical.

Professionals report all of the decision values for the managerial expense and revenue decisions to be more ethical than the students (Table 3). This finding is anticipated based on prior studies (Nash 1990; Axline 1990; Van Der Wal 2011) that explain as managers gain experience in ethical decision making, nuances begin to influence and mediate their judgment. Said another way, professional can see the shades of gray and decisions are not just black or white thus they lose the ethical idealism common to students and become more realistic. The managerial expense manipulation scenarios could be judged to be either questionable management practices or questionable ethics. Because of their experience, practitioners may have read these scenarios as questions of management practice rather than questions of ethics thus judging them to be less unethical than did the students.

Other than the accounting recognition decisions (Scenarios 4, 9, and 11) that found no significant difference between the ethical acceptability of the students and professionals, all other accounting decisions were reported as being more ethical by the students and less ethical by the professionals.

Given the differences in levels of ethical acceptability reported by students and professionals, additional analysis was employed to identify the demographic variables that explain the differences (Table 4). Years of work experience reported by the professionals most often explain their more ethical managerial decisions. Student status and type of employment more often explained the students' greater unethical value regarding accounting recognition decisions. This reinforces the ability of the practitioners

to be aware of the serious valuation impact of the scenarios on the accounting financial reports.

LIMITATIONS

This study explores the ethical decisions made by accounting professionals and students who aspire to become accounting professional in the East Texas region. The findings are tentative due to a number of limitations. First the scenario questionnaire format incorporated only 13 short scenarios. Some of the response differences may have been the result of assumption differences made by the respondents. For example, was the scenarios description within the manager's responsibility? Perhaps smaller variances in responses would have occurred had the scenarios provided more information and content. Second, the population may not be representative for generalization. The professionals represent only regional East Texas CPA firms. No national (big-4) firm representatives were among the respondents. However, industry, manufacturing and educational CPAs were among the respondents. In addition, no students from private higher education institutions with an academic accounting program were a part of the study. The findings may not be representative of a state or national population. However, they would be generalizable to a comparable regional location. And third, although the responses were anonymous, some response bias may be present in the responses.

CONCLUSION AND FUTURE RESEARCH

This study confirms prior studies (Burns and Merchants 1990; Merchant and Rockness 1994; Grasso et al. 2009) that find that practitioners and students have a greater ethical acceptability for operating manipulations than for accounting manipulations. This could be based on the accounting profession's concern with ethical codes and generally accepted accounting practices that does not exist for the managerial activities. Accounting standards seek to ensure that financial reports provide an appropriate reflection of the organization's economic status and thus reflect an institutionalization of ethical concern for honesty. The respondents' greater unethical acceptability of the scenarios may reflect this concern.

This study also demonstrates that accounting professionals and accounting students have ethical sensitivity to questionable managerial and accounting recognition situations but the sensitivity level is uneven. Given the importance of accurate, relevant and reliable information to maintaining the public trust in the accounting profession, this study provides evidence that the educational programs must expand efforts to ensure students are exposed to real world situations in which managers make business decisions. Students, as well as professional accountants, must appreciate the creativity and effectiveness that managerial decision making requires and not rely solely on explicit policy restrictions or accounting guidance. In fact, ethics and personal integrity are a major issue in everyday business decisions.

This study provides some understanding of the ethical value choices. However nothing is available about the basis of the respondents' judgments. Issues such as why the ethical value was selected provide motivation for future research. More can be done as future studies could employ more extensive descriptions of manipulative accounting practices in any number of situations such as financial institutions, markets, or service industries. Future studies could also query a much larger, more expansive, population which would allow robust analysis including differences among professionals.

REFERENCES AND TABLES

References and tables are available upon request to the first author.