

# *Understanding Accounting Ethics*

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## Basics of Accounting Ethics

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## Main Topics

- Professionalism
- Public Interest
- The Virtues of an Accountant
- The Importance of Culture

# Accounting is a Profession

“As professionals, certified public accountants perform an essential role in society. Consistent with that role, members of the American Institute of **Certified Public Accountants** have **responsibilities to all those who use their professional services**. Members also have a continuing responsibility to cooperate with each other to improve the art of accounting, maintain the **public's confidence**, and carry out the profession's special responsibilities for **self-governance**. The collective efforts of all members are required to maintain and enhance the **traditions** of the profession.” AICPA PPC 52.01

# Accounting is a Profession

Key points from 52.01:

- CPAs
  - Play an essential role in **society**
  - Have responsibilities to **ALL users** of their services
  - Have a responsibility to cooperate in maintaining the **public's confidence**
  - Have a responsibility to carry out the responsibility of **self-governance**
  - Must collectively work at maintaining and enhancing the **traditions** of the profession.

# Professionalism Requires Sacrifice

“Obviously no one can claim to be a member of a profession, or expect to succeed in one, unless he is prepared, when necessary, to subordinate his own interest to that of his client.”— George O. May (in “The Accountant and the Investor”, 1932)

**Service is more important than profit**

# Professionalism Requires Altruism

“The high-minded accountant who undertakes to practice in this field assumes high ethical obligations, and it is the assumption of such obligations that makes what might otherwise be a business, a profession. Of all the group of professions which are closely allied with business, there is none in which **the practitioner is under a greater ethical obligation to persons who are not his immediate clients**; and it is for this reason I believe accounting ought, and can be made, to take an outstanding position in this group.” —George O. May (in “The Accountant and the Investor”, 1932)

# Professionalism Requires Altruism

## Practitioners Assume High Ethical Obligations

- Great ethical obligation to persons who are not immediate clients (Public)
- Converts a business to a profession

# The Essence of a Profession: It Aims at an 'Honorable Good'

- An **honorable good** is incommensurably higher than **instrumental goods**.
- **Commensurability**: Two goods are commensurable, if it is meaningful to say that the one good has a value that is some multiple of the other good.

# The Distinction between an Honorable and an Instrumental Good

## Instrumental good:

- Any good which serves as an instrument or provides some comfort or assistance to the body, its appearance or needs.

## Honorable good:

- Any good which is what instrumental goods are for, or which is a precondition of an instrumental good being good at all.

# The Distinction between an Honorable and an Instrumental Good

- Instrumental Good - Examples:
  - Food
  - Clothing
  - Shelter
  - Transportation
- Honorable Good - Examples:
  - Knowledge
  - Health
  - Education
  - Freedom
  - Public Trust

# The Distinction between an Honorable and an Instrumental Good

Honorable goods are preconditions for  
instrumental goods

# Professions Are Correlated with Honorable Goods

*'Honorable good'*

*Corresponding Profession*

Knowledge

Teacher/Professor/Researcher

Justice

Law

Health

Medicine

Freedom, Rights

Public Service

Public Trust

Accounting

# Public Accounting Provides Honorable Goods

Accounting is a Profession because it aims at providing the honorable goods of :

## Knowledge:

- Verifies that some presentation of the position of a company is accurate and representative

## Trust:

- A precondition of the good operation of the market place

# Integrity

The practice of a profession is marked by integrity

Integrity:

- Adherence to moral and ethical principles; soundness of moral character; honesty.

Random House Webster's Unabridged Dictionary

# The Practice of a Profession is Marked by 'Integrity'

“It is painful to have to disagree with those by whom one has been retained, and the person in whose interest one does so is unlikely ever to know what has been done or to appreciate the stand that has been taken on his behalf. **But in the long run, the willingness of an accountant to do what he conceives to be his duty to the unknown investor, even if by so doing he alienates a client and suffers a present loss of business, brings a rich reward both in self-respect and in a professional reputation which, in turn, brings a pecuniary benefit.**”

George Oliver May ( in “The Accountant and the Investor”, 1932)

# Three Marks of Integrity

1. Disinterested service.
2. Self-regulation, both corporately and personally.
3. Interweaving of ethical commitment and professional service.

# First Mark of Integrity: Disinterested Service

**Self-interest**, in the form of economic advancement, should be an **incidental aim** in the work of a professional, and a professional should always be prepared to **sacrifice self-interest** to attain the good that he or she aims to provide.

# First Mark of Integrity: Disinterested Service

- The payment that a professional receives for services has more of the character of an **honorarium** or stipend than a strict equivalent.
- Strictly, the work of a professional cannot be compensated for by money, because money is only an instrumental good, but a professional provides an incommensurably higher good.

# Second Mark of Integrity: Self-Regulation

- Contrast with someone who provides an instrumental good. Such a person is strictly working at the service and on the demand of someone else.
- A profession is self-regulating both **corporately** and **individually**.

# Self-Regulation

- Corporately:
  - The profession is responsible for :
    - Setting high standards
    - Enforcing high standards
- Individually:
  - A professional must constantly rely of his or her **judgment** in applying ethical principles to daily circumstances.

# Third Mark of Integrity: Inherently Ethical Framework

- The entire orientation and outlook of a professional should attest to the priority of its honorable' good over instrumental goods.
- “The Principles call for an unswerving commitment to **honorable behavior**, even at the **sacrifice of personal advantage**” (Preface to AICPA Code of Conduct, 51.02).

# Integrity

- Integrity is measured in terms of what is **Right** and **Just**...
- ...In the absence of specific rules, standards, or guidance, or in the face of conflicting opinions, a member should **test decisions and deeds** by asking: “**Am I doing what a person of integrity would do? Have I retained my integrity?**”...

# Integrity

- ...Integrity requires a member to observe both the **Form** and **Spirit** of technical and ethical standards; circumvention of those standards constitutes **subordination of judgment**. AICPA PPC 54.03

# Public Interest and the Distinctive Work of an Accountant

- The distinctive work or contribution of an accountant is **securing the conditions of trust**.
- “A distinguishing mark of a profession is **acceptance of its responsibility to the public**. The accounting profession's public consists of clients, credit grantors, governments, employers, investors, the business and financial community, and others who rely on the **objectivity** and **integrity** of certified public accountants to maintain the **orderly functioning of commerce**. This reliance imposes a **public interest responsibility** on certified public accountants” (53.01).

# Public Interest and the Distinctive Work of an Accountant

Distinctive work of CPAs:

- Secure the condition of Trust

Distinguishing mark of a profession:

- Acceptance of responsibility to the public

# What an accountant must do to carry out this distinctive work well

1. Maintain himself or herself in circumstances in which there are not any inducements or incentives to misrepresent the financial position of a firm.
2. Have sufficient skill to be able to assess and make a judgment about the represented financial position of a firm.
3. Seek information and carry out the investigation to the extent that is necessary.
4. Having a concern with what a creditor or investor would find relevant; and then,
5. Actually arriving at a fair and a reasonable judgment as regards the represented financial position of a firm; and,
6. Expressing this judgment in language which allows a third party naturally to form the same judgment.

# These imply the virtues of an accountant

Maintain himself or herself in circumstances in which there are not any inducements or incentives to misrepresent the financial position of a firm. =

**Independence**

## Virtues of an Accountant

Have sufficient skill to be able to assess and make a judgment about the represented financial position of a firm.=  
**Competence.**

## Virtues of an Accountant

Seek information and carry out the investigation to the extent that is necessary, in view of his having a concern with what a creditor or investor would find relevant.= **Due Care (Empathy)**

## Virtues of an Accountant

Having a concern with what a creditor or investor would find relevant. = **Regard for the Public Interest.**

## Virtues of an Accountant

Actually arriving at a fair and a reasonable judgment as regards the represented financial position of a firm; and expressing this judgment in language which allows a third party naturally to form the same judgment. = **Objectivity**

# The six distinctive virtues of an accountant

- Concern for Maintaining **Independence**
- **Competence** and Sense of Limits
- **Due Diligence** (Due Care)
- Sense of the **Public Interest**
- **Objectivity** (Sound Judgment)
- **Integrity** (Professionalism)

# Independence

“As a practical rule, an accountant should run no risk of putting himself in a position where his interest might with any reason be thought to be large enough to affect his judgment, and it is the part of wisdom to resolve all doubts on such a question conservatively by **declining the doubtful appointment**”.—George O. May

- Independence (**the condition**): The condition of being free of incentives or inducements that would work to deflect judgment.
  - External attacks on (the condition of) independence: **conflicts of interest.**
  - Internal attacks on (the condition of) independence: **greed; bad character.**
- Independence (**the virtue**): Valuing independence (the condition) above one's own interests and habitually taking care to achieve independence.

# Independence

- Accounting distinctively provides trust
- Trust implies trustworthiness
- That someone is trustworthy is a matter of **PERCEPTION**
- CPAs
  - Must **be** trustworthy, and
  - They must **appear** trustworthy
- Therefore, CPAs must avoid anything that would make them **SEEM** not to be trustworthy.

# Even the appearance of a lack of independence must be avoided

- “Independence precludes relationships that may appear to impair a member's objectivity in rendering attestation services.” AICPA Code 55.01
- “Such a member who provides auditing and other attestation services should be independent in fact and appearance.”  
55.03

The importance of the appearance of independence for the trust placed collectively in the accounting profession

“Members also have a continuing responsibility to cooperate with each other to improve the art of accounting, maintain the public's confidence, and carry out the profession's special responsibilities for self-governance. The collective efforts of all members are required to maintain and enhance the traditions of the profession.”

AICPA Code 52.01

# Objectivity

“I believe that every high-minded accountant has accepted the principle that, once his conclusions are reached, the report or certificate which he issues, and which is designed to influence action, must be so worded that not only will every statement made therein be literally true, but every inference which could legitimately be drawn from the language will be warranted by the facts. There is no place in accountants’ certificates for what President Roosevelt once called ‘weasel words’.” —George O. May ( in “The Accountant and the Investor”, 1932)

# Objectivity in Thought and in Expression

- **Transparency**: a trait of a communication, where what that communication is naturally understood as saying is a fair representation of what one is making a judgment about.
- **Objectivity in thought**: an impartial, honest, and fair state of mind.
- **Objectivity of expression**: transparency.

# Objectivity of Expression

What one says or writes is **naturally** and

**reasonably** understood in such a way as that

it conveys an **accurate representation**

# Culture

- The term ‘culture’ refers to the broad set of conditions that make it easy to **acquire certain habits of action** and to live in a certain way.
- ‘Culture’ in an accounting firm is not something that can be fostered by a single practitioner alone; this is primarily the responsibility of senior partners—the so-called **‘tone at the top’**.
- A Code of Conduct is useful for fostering a culture.

# When is a Code of Conduct Actually Implemented?

- There is some procedure in place which guarantees that practitioners **study** and **understand** it.
- There are **incentives** for the good observance of the code.
- The code is '**enforced**', that is, practitioners are in the habit of encouraging one another to observe it; **they expect others to follow it**; and egregious violations are reported and dealt with appropriately.

**ETHICAL BEHAVIOR IS  
NOT AN OPTION**