RESEARCH ON PROFESSIONAL RESPONSIBILITY AND ETHICS IN ACCOUNTING

VOLUME 11

CYNTHIA JEFFREY

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ISSUES RELATING TO TEACHING ACCOUNTING ETHICS: AN 18 YEAR RETROSPECTIVE

Stephen E. Loeb

ABSTRACT

This paper reconsiders three issues concerning teaching ethics to accounting students in colleges and universities discussed in Loeb (1988). A number of changes that relate to accounting ethics education that have occurred since 1988 are discussed. The current need for ethics education in accounting programs in higher education is reviewed. Consideration is given to the goals of ethics education in accounting and the operationalization of those goals. The issue of who should teach ethics in accounting programs in colleges and universities is discussed. A number of comments and suggestions are made relating to the teaching of ethics in the curriculum of accounting programs in institutions of higher education.

In the late 1980s, factors such as the Treadway Commission (1987, see pp. 16, 82, 83) report and an American Accounting Association (AAA) committee report (AAA, 1986, p. 179) suggested the need for more attention to ethics education in accounting (see, e.g., Loeb, 1988, pp. 316–317; 1993, p. 53; Loeb & Rockness, 1992, p. 485). During that time period, one of my papers (Loeb, 1988) considered "three crucial issues [in] the classroom

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teaching of accounting ethics" (p. 317). More specifically, in that paper I (1988, p. 317) considered (a) "the need for classroom teaching of accounting ethics in colleges and universities," (b) "the goals" of such "teaching," and (c) "the individuals who should" do such teaching. As discussed later, in the late 1980s, there was likely a limited amount of formal teaching of accounting ethics in higher education. Since the publication of Loeb (1988), a number of authors, including myself, have commented on various issues related to accounting ethics education (see, e.g., Langenderfer & Rockness, 1989; Cohen & Pant, 1989; Armstrong & Mintz, 1989; Loeb, 1990, 1991, 1993, 1994, 1998; Loeb & Rockness, 1992; Thompson, McCoy, & Wallestad, 1992; Huss & Patterson, 1993; Geary & Sims, 1994; Kerr & Smith, 1995; Stewart, 1997; Douglas & Schwartz, 1998; Esmond-Kiger & Stein, 1998; Gunz & McCutcheon, 1998; Knapp, Louwers, & Weber, 1998; D'Aquila, 1999; Bracken & Urbancic, 1999; Madison, 2001; Armstrong, Ketz, & Owsen, 2003; Haywood, McMullen, & Wygal, 2004; Earley & Kelly, 2004; Jennings, 2004; Thomas, 2004; Abdolmohammadi, 2005; VanZante & Ketcham, 2005; Dellaportas, Leung, Cooper, & Jackling, 2006; Van Peursem & Julian, 2006).

Approximately 18 years have passed since the publication of Loeb (1988). Since 1988, the AAA's Professionalism and Ethics (P & E) Committee for a limited number of years sponsored seminars on the teaching of accounting ethics and also developed a number of ethics cases (see, e.g., Loeb & Rockness, 1992, pp. 486–487; Loeb, 1993, p. 53). As noted later, in more recent years the AAA P & E committee has sponsored ethics research symposiums.[1] Evidence considered below suggests that over the last 18 years there has been an increase in the teaching of ethics in some accounting programs in colleges and universities in the United States (U.S.). This increase in accounting ethics education, the recent business ethics crises (discussed below), and the passage of time since the publication of Loeb (1988) suggest the appropriateness of a reconsideration of the three crucial issues raised in Loeb (1988).

In 1990, I developed and began teaching a course relating to ethics and professionalism in accounting, and in 1993, began an extensive involvement with the teaching of business ethics (see Loeb, 1998, p. 236).[2] In this current paper, I draw upon my many years of teaching accounting ethics and my involvement with business ethics education to reconsider the three crucial issues raised in Loeb (1988). As a result, I make a number of comments and suggestions relating to the teaching of ethics in accounting programs in colleges and universities in the U.S. While the focus of my paper is on ethics education in colleges and universities in the U.S., my comments and suggestions may have implications for ethics education in colleges and

universities in other nations. Additionally, I comment on certain international developments that may have implications for ethics education in accounting programs in colleges and universities in the U.S.

In the next section, I discuss a number of changes that have occurred since 1988 that have impacted ethics education in accounting programs in colleges and universities in the U.S. I follow this with a reconsideration of the need for accounting ethics education in colleges and universities in the U.S. Next, I consider the goals of accounting ethics education which is followed by a discussion of operationalization of those goals. I then consider who should teach ethics in an accounting program. This is followed by a final discussion and conclusions.

CHANGES SINCE 1988

Since 1988, a number of changes have occurred that have affected accounting ethics education in colleges and universities in the U.S. These changes include: (a) the establishment of the AAA P & E Committee and its subsequent activities, (b) the increased coverage of ethics in some accounting programs in institutions of higher education in the U.S., (c) the recent business ethics crisis, and (d) the increase in research relating to accounting ethics.

The AAA P & E Committee

The AAA P & E Committee was established in 1988 (see Langenderfer, 1990, p. i). The Committee, benefiting from generous financial support from private sources, for a limited number of years held annual seminars on accounting ethics education, developed material for use in accounting education, and took other actions to promote ethics education in accounting (see, e.g., Loeb & Rockness, 1992, pp. 485–487; Loeb, 1993, pp. 53, 56). In the mid-1990s, the Committee began to sponsor an annual research symposium (see "Call for Papers: Professionalism and Ethics Committee, Symposium on Ethics Research in Accounting," 1995, p. 5). The 10th AAA Ethics Research Symposium was held in San Francisco in August of 2005.

Increased Coverage of Ethics in some Accounting Programs in the U.S.

Evidence of Increased Coverage

An empirical study conducted by Cohen and Pant (1989) suggests that during the late 1980s coverage of ethics in accounting programs in higher

education was limited (also see, e.g., Treadway Commission, 1987, pp. 82–83; Wyer, 1987, p. 108; Karnes & Sterner, 1988, pp. 21–22; Armstrong & Mintz, 1989, p. 74; Thompson et al., 1992, pp. 95–99; Loeb & Rockness, 1992, pp. 485, 488; Armstrong, 1993, p. 78). Cohen and Pant (1989, pp. 79–80) conclude "that, with the exception of auditing, the current coverage of ethics in accounting courses is minimal." However, evidence discussed below suggests that the coverage of ethics in some accounting programs in colleges and universities in the U.S. has increased in the last 18 years.

Madison (2001) reports the results of a survey of existing accounting ethics education "in … accounting programs [in] colleges and universities" in the state of Ohio (p. 39). Madison (2001) indicates that among responding programs "an average of 9.5[5] hours of ethics instruction" was reported in various undergraduate accounting courses (p. 41; also, p. 41, Exhibit D). Haas (2005), writing about a survey of "department chairs" at "colleges in New York State … that grant associate's and bachelor's degrees in accounting" (p. 67), reports (pp. 67–68) responses that suggest that a number of students in accounting programs were receiving some type of exposure to ethics. Mastracchio (2005, pp. 6, 8) cites evidence that suggests some accounting programs include ethics in their curriculum.

There is evidence that ethics is included in a number of accounting textbooks that are used in various accounting courses in colleges and universities (see Loeb & Rockness, 1992, p. 488; Loeb, 1993, pp. 54, 56). D'Aquila (1999, p. 21) notes that "almost every accounting textbook incorporates business ethics." Also, Bracken and Urbancic (1999, e.g., pp. 279, 280) studied the inclusion of ethics in a number of books used in courses in introductory accounting. Bracken and Urbancic (1999, pp. 280–284) found that the textbooks in their study contained a good deal of material relating to ethics and the ethics coverage was in a variety of formats.

In recent years, at least two states have adopted an ethics course prerequisite for applicants wishing to take the CPA examination (CPA candidates). More specifically, since July 1, 1999, Maryland has required CPA candidates to have a course in business ethics and Texas began a somewhat similar requirement in 2005 (see, e.g., Loeb, 1998, pp. 247–248; Abdolmohammadi, 2005, p. 39; VanZante & Ketcham, 2005, p. 13). At a minimum, the board of accountancy initiatives in both Maryland and Texas help assure increased coverage of ethics in accounting programs within their own jurisdictions (see the discussion in 2003–2004 P & E Committee, 2004, especially the Appendix).[3] These requirements are important milestones in efforts to increase coverage of ethics in accounting education in colleges and universities in the U.S.

Suggestions for Wider Coverage
Notwithstanding the progress noted in the previous section of this paper concerning the inclusion of ethics education in accounting programs in colleges and universities in the U.S., it is likely that the inclusion of ethics in the accounting curriculum is not universal and furthermore the degree of its inclusion likely is highly variable. For example, Frecka and Nichols (2004, see pp. 167–169), reporting the results of a survey in which there were responses from "42 graduate accounting programs" (p. 167), note that "there are few courses specifically devoted to developing personal competencies such as objectivity, honesty, and ethics" (p. 183). Also, Watkins and Iyer (2006, p. 68), after reviewing the websites of Association to Advance Collegiate Schools of Business International accredited accounting programs, suggest that the coverage of ethics was not sufficient in a number accounting programs reviewed.

2003–2004 AAA P & E Committee Letter. The 2003–2004 AAA P & E Committee, of which I was a member, prepared a letter to the National Association of State Boards of Accountancy (NASBA) and the AAA sent the letter to NASBA (2003–2004 P & E Committee, 2004). The letter, which reflected only the 2003–2004 AAA P&E Committee's opinion, expressed that Committee's support for individual board of accountancy ethics educational requirements for CPA candidates (see 2003–2004 P & E Committee, 2004).

NASBA Exposure Draft. More recently, a NASBA exposure draft proposed a number of changes to the rules relating to education of the Uniform Accountancy Act (UAA), including changes that likely would have resulted in a more intensive coverage of ethics in a number of college and university accounting programs in the U.S. that educate students who are interested in becoming CPAs (see, e.g., NASBA, 2005; Reckers, 2006, pp. 33–34).[4] NASBA received a number of comments on the exposure draft.[5] At this writing, NASBA has tabled the exposure draft and established a task force that is charged with reviewing what has transpired on the issue, developing educational recommendations, and asking for comments from relevant interested parties (see, e.g., NASBA, 2006a; NASBA Education Task Force, 2006, pp. 1, 5; Rayburn, 2006, p. 1).

Individual boards of accountancy are not required to adopt NASBA CPA candidate-related education standards (see Reckers, 2006, pp. 33, 39–40; also, see the discussion in Rayburn, 2006, p. 1). However, NASBA recommended education standards for CPA candidates may be viewed as best

practices and thus may influence the education standards of individual boards of accountancy.[6] Thus, the UAA education standards that result from the current process may over time impact the CPA candidate-related education standards of a number of boards of accountancy and consequently the accounting curriculum in a number of colleges and universities in the U.S. (see the discussion in Reckers, 2006).

In early 2006, the NASBA task force issued and requested comments on a "Framework for Revision – Rules 5–1 and 5–2" that, among other matters, included two options for an ethics education requirement for CPA candidates (NASBA Education Task Force, 2006, pp. 4–5). The first option was a freestanding three semester-hour ethics course. The second option was six semester-hours of ethics which the wording suggests can be in the form of two three semester-hour ethics courses or one three semester-hour course and an additional three semester-hours earned by integrating ethics in various courses in the curriculum (see NASBA Education Task Force, 2006, pp. 4–5).[7]

International Federation of Accountants. NASBA is a member organization of the International Federation of Accountants (IFAC) (IFAC, 2006a). In 2003, the IFAC, through its Education Committee, issued six "International Education Standards for Professional Accountants (IES)" (IFAC Education Committee, 2003h, p. 5; 2003a, see the table of contents).[8] All six standards (IESs) became effective on January 1, 2005 (IFAC Education Committee, 2003a, pp. 38, 43, 54, 61, 68, 75). IES 1 (IFAC Education Committee, 2003b), IES 3 (IFAC Education Committee, 2003d), IES 5 (IFAC Education Committee, 2003f), and IES 6 (IFAC Education Committee, 2003g) discuss or mention ethics and professionalism at various points. However, IES 2 (IFAC Education Committee, 2003c) which discusses accounting program "subject" (see, e.g., p. 46) coverage and IES 4 (IFAC Education Committee, 2003e) which is devoted to the issue of accounting ethics and professionalism education are especially crucial in their support of accounting ethics education. Ultimately, as suggested below, all six of these standards, especially IES 2 and 4, may encourage and/or result in more coverage of ethics in accounting programs in colleges and universities in the U.S.

In addition to IESs, IFAC Education Committee (2003h, pp. 5–6) in paragraph 15 notes that the Education Committee can issue "International Education Guidelines for Professional Accountants (IEG)" and "International Education Papers for Professional Accountants (IEP)." Paragraph 16 notes that IESs have the most authority, followed in order of authority by

IEGs and then IEPs (IFAC, 2003h, p. 6). Also, in paragraph 16, IFAC Education Committee (2003h, p. 6) indicates that IESs "prescribe good practice," IEGs provide assistance in complying with IESs, and IEPs provide discussion of various matters and provide results (IFAC Education Committee, 2003h, p. 6).

As discussed below, IES 2 and IES 4 provide strong positive support for accounting ethics education. Given the position taken by IES 1–6, especially IES 2 and IES 4, in strongly advocating accounting ethics education, what effect can these standards have on accounting programs in colleges and universities in the U.S? Dellaportas et al. (2006, p. 5) raise the issue as to whether compliance with an International Federation of Accountants IES is "mandatory" for IFAC member organizations. In addressing this question, Dellaportas et al. (2006, p. 5) refer to IFAC Education Committee (2003h, 2003i) and the discussion in the next paragraph follows their approach.

IFAC Education Committee (2003h, p. 2) in paragraph 4 notes that "IFAC expects member bodies to comply with" IESs (also see IFAC Education Committee, 2003i, p. 26). However, the IFAC Education Committee (2003h, p. 3) in paragraph 5 notes that IESs "cannot override authoritative local pronouncements." Further, IFAC Education Committee (2003h, p. 3) in paragraph 7, while noting that existing "laws" and "regulations" take precedence over IESs, requires member organizations (a) to consider IESs and IEGs when dealing with education issues, (b) to make public policy makers aware of IESs and IEGs, and (c) to work to "harmonize" laws and regulations with IESs and IEGs (also see IFAC Education Committee, 2003i, p. 26).[9]

IES 2 in bold type-face specifies "subject areas" for inclusion in a professional accounting program (IFAC Education Committee, 2003c, pp. 43–44, 46, 47, 49). Bold type-face signals that the content in bold are standards (see Note 9). Among the subjects included in IES 2 in bold faced-type are "professional values and ethics" (paragraph 23) (IFAC Education Committee, 2003c, p. 46), "corporate governance" (paragraph 25), and "business ethics" (paragraph 25) (IFAC Education Committee, 2003c, p. 47). While IES 2 specifies the subjects for inclusion in a professional program, IES 2 in paragraph 22 suggests that it is the responsibility of member organizations and relevant public policy makers to establish "the relative depth and weighting of coverage" for the subjects (IFAC Education Committee, 2003c, p. 45).

Paragraph 1 of IES 4 indicates that a goal of IES 4 is to specify the elements of ethics and professionalism that should be learned as part of an individual's education taken in preparation to obtaining a professional

accounting "qualification" (IFAC Education Committee, 2003e, p. 60). Paragraph 8 of IES 4 suggests that ethics and professionalism be considered a mainstream subject in the accounting educational process (IFAC Education Committee, 2003e, p. 61). Then, in paragraph 9, IES 4 distinguishes "between teaching … about" ethics and professionalism and "developing and instilling ethical behavior" (IFAC Education Committee, 2003e, p. 61). Paragraph 9 suggests that this development should start early in the education process which seems to imply that changed behavior should be one of the outcomes of accounting education (see IFAC Education Committee, 2003e, p. 61; also see Dellaportas et al., 2006, p. 7).

In paragraphs 13–16, IES 4 discusses the ethics and professionalism educational content, and in paragraphs 17–22, IES 4 discusses ethics education issues such as a separate ethics course versus integration of ethics into the curriculum (see Note 15) and instructional techniques to be used to teach ethics (IFAC Education Committee, 2003e, pp. 63–64). Finally, in paragraphs 23–27, IES 4 discusses ethics and professionalism education in a work setting (IFAC Education Committee, 2003e, pp. 64–65). The content coverage in paragraphs 13–16 of IES 4 is both extensive and in bold typeface (see IFAC Education Committee, 2003e, pp. 62–63). Thus, paragraphs 13–16 as well as the rest of IES 4 provide strong positive support for accounting ethics education.

NASBA is a member organization of IFAC and thus is expected to support IES 1–6 in the manner discussed earlier (see the discussion in Dellaportas et al., 2006, p. 5). As noted above, IES 1–6, especially IES 2 and IES 4, provide strong positive support for ethics education in accounting programs leading to qualification of an individual as a member of the accounting profession. Thus, IES 1–6, especially IES 2 and 4, and any IEGs that may be issued in the future that are related to IES 4, have the potential to affect NASBA's current deliberations concerning what, if any, ethics education should be included in NASBA's UAA education standards. As suggested earlier, the UAA education standards may affect the CPA candidate-related education standards of individual boards of accountancy, which in turn can affect the accounting curriculum in colleges and universities in the U.S. Consequently, IES 1–6, especially IES 2 and IES 4, and any IES 4 related IEGs, over time, may be factors in increasing the demand for ethics education in accounting programs in colleges and universities in the U.S.[10]

My Preference. My preference, if there is to be an ethics education standard for CPA candidates in the U.S., is to require one freestanding three

semester-hour business ethics or accounting ethics course in a college or university (cf., e.g., Loeb, 1998, p. 247; 2003–2004 P & E Committee, 2004; Fisher & Swanson, 2005; Shaub, 2006). The current Maryland and Texas education requirements are examples of such an approach. Also, my preference is concomitant with the first option of the NASBA task force's "Framework for Revision – Rules 5–1 and 5–2" (NASBA Education Task Force, 2006, pp. 4–5).

Professional or regulatory requirements can place strong pressure on academic institutions to include ethics in their curriculum. For example, Bok (1988, p. 5) notes that in legal education "instruction in professional responsibility is mandatory thanks to the American Bar Association." Earlier I noted that, at a minimum, the board of accountancy initiatives in Maryland and Texas help assure increased coverage of ethics in accounting programs within their own jurisdictions (see the discussion in 2003–2004 P & E Committee, 2004, especially the Appendix). Thus, I think it is essential that NASBA have some type of ethics education requirement as part of its education standards. I think a three semester-hour freestanding ethics course requirement, if adopted by individual boards of accountancy, would encourage college and university accounting programs in the U.S. to include ethics in the curriculum (see the discussion in 2003–2004 P & E Committee, 2004). If individual boards of accountancy so decide, more than three semester-hours of ethics education could be required. However, in the long term, a requirement of one three semester-hour ethics course would help assure that ethics education will be an integral part of the curriculum for most, if not all, college and university accounting programs in the U.S.

Recent Business Ethics Crisis

In the later part of the 20th century and the early part of the 21st century some business ethics problems have occurred. In this current paper I refer to these problems as the "recent business ethics crisis." This recent business ethics crisis has, in part, resulted in the enactment of the Sarbanes Oxley Act (SOX) and with that law the establishment of the Public Company Accounting Oversight Board (PCAOB).

Increase in Accounting Ethics Research

Previts and Merino (1998, pp. 339–340) note the paucity of research on the "development of ethical standards and the enforcement of codes of ethics" before 1973. While I believe that academic accounting ethics research in

these areas and academic accounting ethics research in general have increased in the years thereafter, I sense by 1988 there still was not a large amount of academic research on accounting ethics topics (see, e.g., the discussion in Previts & Merino, 1998, pp. 339–340; Gunz & McCutcheon, 1998, p. 1151; Bernardi, 2005). Bernardi (2005) reviews the 1968 to 2002 contents of 22 publication outlets (see pp. 63, 67, 87–88). Bernardi (2005) provides evidence that some accounting scholars are conducting ethics research. However, the findings presented in Bernardi (2005) suggest that the number of scholars conducting ethics research is not overwhelming.[11]

In Loeb (1988, p. 326), I suggested that ‘‘ethics’’ was not viewed as a ‘‘primary [area] of [accounting] teaching and research’’ and that doing both was ‘‘a risky career strategy.’’[12] My sense is that it is still somewhat risky for an accounting academic to focus on ethics, particularly early in an individual's ‘‘career’’ (see the discussion in Loeb, 1988, p. 326; Gunz & McCutcheon, 1998, p. 1152; Haas, 2005, p. 68). Notwithstanding such risk, there are today a number of accounting academics conducting research in accounting ethics (see Bernardi, 2005; Bernardi, Bean, & Williams, 2005). Currently, the work of these scholars is facilitated by a fairly large number of academic and practitioner journals that publish articles relating to accounting ethics (see, e.g., Gunz & McCutcheon, 1998, p. 1152; Bernardi, 2005, pp. 66–68, 91; Bernardi et al., 2005, pp. 174–176).

The increase of faculty conducting research in the area of accounting ethics and the fairly large number of journals that will publish papers relating to accounting ethics likely is attracting scholars to accounting ethics research. The increase in scholars conducting research in the areas of accounting ethics in turn facilitates the teaching of accounting ethics (cf., Bean & Bernardi, 2005, p. 65). My reasoning here is that faculty members conducting research on accounting ethics are likely excellent candidates to teach accounting ethics. The development of accounting ethics as a research field will become even more crucial if, as I raise the possibility earlier and later in this paper, the demand for the teaching of accounting ethics substantially increases.

NEED FOR ACCOUNTING ETHICS EDUCATION

I believe that the need for accounting ethics education in colleges and universities in the U.S. has not diminished in the years since 1988. The practice of accountancy has increased not decreased in complexity. Since 1988, the number of accounting standards has increased and the enactment of SOX

and the establishment of the PCAOB have made the accounting work environment more complex. Furthermore, the recent business ethics crisis suggests the need for a greater emphasis on ethics in the education of accounting students in U.S. colleges and universities. Ethics education can assist accounting students in their understanding of the need for compliance with professional standards and, as discussed below, prepare students to deal with ethical conflicts that they eventually may encounter in practice (see Loeb, 1988, pp. 317–319).[13] Thus, in my view, nothing has occurred since 1988 to suggest that the need for teaching ethics in college or university accounting programs has lessened.

THE GOALS OF ACCOUNTING ETHICS EDUCATION

Four Essential Goals

In Table 1 of Loeb (1988, p. 322), I suggested seven "Possible Goals of Accounting Ethics Education" that I noted were "adapted from Callahan [1980, pp. 64–74]" (Loeb, 1988, p. 321; also see, Loeb, 1988, pp. 320–321; 1990, p. 283, n. 9; 1991, p. 78; 1993, p. 54, n. 13; 1994, pp. 819, 825, n. 15; 1998, p. 238). These goals are listed in this current paper in Table 1.

Then in Loeb (1993, pp. 53–54), I suggested that of these seven goals, goals #2 (recognition), #4 (development of capability), #5 (uncertainty), and #6 (preparing) were "sufficient for effective accounting ethics education." (p. 54). While all seven goals noted in Table 1 are important, my work over the last 18 years suggests that goals 2, 4–6 are essential to successful teaching of ethics to accounting students. While goals 1, 3, and 7 also are important, I will point out that these three goals, in large part, can be addressed as part of one or more of the other four goals that I view as essential. Goals 2, 4–6 are interrelated (see below) and should be considered when initially designing ways to include ethics in the accounting curriculum in a college or university (see the discussion in Loeb, 1993, p. 54). A brief discussion of these four essential goals will highlight their importance to successful accounting ethics education.

Recognition (Goal #2)

Accounting practitioners should have the ability to "recognize" when they have encountered a situation "that [has] ethical implications" (Loeb, 1988, p. 321; 1988, p. 322, Table 1; also see Table 1; Loeb, 1993, p. 54). Thus, goal #2 focuses on educating students to recognize situations "that have ethical

implications'' (Loeb, 1988, p. 321; 1988, p. 322, Table 1; also see Table 1). To address goal #2, an accounting curriculum should expose students to the codes of ethics that have been adopted by professional groups that are part of the accounting profession such as ''the American Institute of Certified Public Accountants'' and ''the Institute of Management Accountants'' (see Loeb, 1998, p. 239). Exposing students to these codes of ethics also addresses, in part, goal #7. Further, the inclusion of ethical theory in the curriculum (see goals 4 and 7) also may increase the ability of students to recognize issues that have ethical implications. Thus, by addressing goal #2 many of the aspects of goal #7 (see Table 1) also are considered. Further, learning to recognize issues with ethics implications facilitates meeting goal #1 (''relate accounting education to moral issues'') (Loeb, 1988, p. 321; 1988, p. 322, Table 1; also see Table 1).

Development of Capability (Goal #4)
When an accounting practitioner encounters and recognizes a matter that has ethical dimensions or implications, the practitioner should able to think through and develop actions pertaining to the situation (Loeb, 1988, p. 321; 1988, p. 322, Table 1; also see Table 1; Loeb, 1993, p. 54). Thus, as suggested by goal #4, the curriculum should provide accounting students with the background to address such matters (see Loeb, 1993, p. 54). Such a background may include the study of ethical theory as well as the suggestion of a process or perhaps alternative processes that students can use in approaching ethical decisions (see, e.g., Loeb, 1993, p. 54). By use of instructional techniques such as case analysis, the curriculum should provide students with opportunities to practice dealing with ethical dilemmas (see Mai-Dalton, 1987, p. 511; Loeb 1988, p. 324). Instructional techniques that have students

Table 1. Goals of Ethics Education in Accounting Suggested in Loeb (1988, p. 322).

''1. Relate accounting education to moral issues.
2. Recognize issues in accounting that have ethical implications.
3. Develop 'a sense of moral obligation' or responsibility.
4. Develop the abilities needed to deal with ethical conflicts or dilemmas.
5. Learn to deal with the uncertainties of the accounting profession.
6. 'Set the stage for' a change in ethical behavior.
7. Appreciate and understand the history and composition of all aspects of accounting ethics and their relationship to the general field of ethics.''

Note: Quoted from Table 1, Loeb (1988, p. 322) where there is a footnote that states: ''This list was adapted from Callahan [1980, pp. 64–74].''

considering accounting issues that have ethical dimensions or implications should also facilitate meeting goal #1 and, as noted earlier, goal #2.

Uncertainty (Goal #5)

The practice of accountancy contains a good deal of uncertainty. Actual business practice may raise accounting issues that do not always exactly fit existing standards (cf., Loeb, 1993, p. 54; 1998, p. 238). Practitioners may be uncertain as to how to approach a particular issue. However, accounting practitioners can research the issue or issues and form a professional position on the matter. The issue or issues may have ethical dimensions or implications and/or there may be ethical dimensions or implications in the way the practitioner approaches the development of his or her position on the issue or issues.

Accounting students should "learn" how "to deal with" such uncertainty and become aware that part of the uncertainty may be due to ethical issues inherent in a problem (Loeb, 1988, p. 321; 1988, p. 322, Table 1; also see Table 1; Loeb, 1993, p. 54). Thus, ethics should be introduced in the accounting curriculum in a manner so that its study will assist students in learning to deal with the uncertainty of practice (see Loeb, 1988, p. 321; 1988, p. 322, Table 1; Table 1; see the discussion in Loeb, 1993, p. 54). Dealing with uncertainty (goal #5) may also assist in addressing goal #1 and goal #2.

Preparing (Goal #6)

In Loeb (1988, p. 321), I note "Callahan [1980, p. 70] contends that an ethics course should 'set the stage for' a change in an individual's behavior" (also see Loeb, 1988, p. 321; 1988, p. 322, Table 1; Table 1). Callahan (1980, p. 70) stresses that ethics education should provide "the student with those ingredients of ethical analysis and self-criticism, such that [the student] would, *if* the analysis seemed to require it, both recognize the importance of changing behavior, and be prepared to change" (emphasis in original). Thus, goal #2 (recognition) and goal #4 (development of capability) will prepare a student to recognize and deal with an ethical conflict situation and also prepare a student for change (see Callahan, 1980, p. 70; Loeb, 1993, p. 54). Also, developing a student's "'sense of moral obligation' or responsibility" (goal #3) (Loeb, 1988, p. 321; 1988, p. 322, Table 1; also see Table 1; Callahan, 1980, pp. 66–67) will help a student deal with an ethical conflict situation and prepare a student for change (cf., Armstrong, 1993, p. 78).

If an individual faced with an ethical conflict situation does not realize that the situation has ethical implications, then the individual cannot change

behavior. Thus, by addressing goals 1 and 2 an accounting student will have a better sense of when a situation has ethical dimensions or implications and be better prepared to change behavior. Other goals also will assist in preparing a student to change his or her behavior. As noted above, goal #3 and goal #4 will be useful in this process. Also, learning to deal with uncertainty (goal #5) and understanding accounting ethics and ethics in general (goal #7) can be useful in preparing for change.

Can Accounting Students Learn Ethics in Colleges and Universities?

In Loeb (1988, p. 321), I cite Callahan (1980, p. 69) who I note ''questions whether'' ethics education should have the goal of ''changing an individual's 'moral behavior.''' Further, as I point out in Loeb (1988, p. 321) and discuss above, Callahan (1980, p. 70) suggests that ethics education can perhaps facilitate a student's readiness to change. As I suggest above, preparing a student for change (goal #6) may be facilitated by addressing the other six goals noted in Table 1 (also see the discussion in Loeb, 1993, p. 54).

Some may raise the question as to whether accounting students can learn ethics in colleges and universities (see, e.g., the discussion in Fess, 1987, p. 60; Geary & Sims, 1994, pp. 3–4, 15–16; Dellaportas et al., 2006, pp. 6–9; Van Peursem & Julian, 2006, p. 15). Questions of this nature, in large part, may be related to the idea that accounting ethics education or ethics education in general should change an accounting student's moral behavior (see Fess, 1987, p. 60; Geary & Sims, 1994, p. 3; Dellaportas et al., 2006, pp. 6–7; Van Peursem & Julian, 2006, p. 15). Callahan (1980, p. 69) suggests that attempting to change how a student behaves ''is an exceedingly dubious goal'' for ethics education (see the discussion in Loeb, 1988, p. 321; 1993, p. 54; Dellaportas et al., 2006, p. 6). Callahan (1980, pp. 69–70) provides arguments to support his position. More specifically, Callahan (1980, p. 69) expresses concern about the durability of ''behavior'' that is learned in a class after the student finishes that class. Additionally, Callahan (1980, p. 69) expresses concern that for students who have not had practical experience there is no behavior that is in need of changing and further there is no assurance that faced with an ethical dilemma that students always would make an unethical choice. Finally, Callahan (1980, pp. 69–70, also see p. 71) suggests that rather than designing a course to instruct a student in how to behave in a particular way in an ethical conflict situation, an ethics course should be designed to assist a student when faced with such an ethical conflict, in how to develop a solution (see the discussion in Dellaportas et al., 2006, p. 6).

I think that over-concern with justifying the existence of accounting ethics education based on measuring whether ethics education is effective in changing students' moral behavior moves the discussion about teaching ethics in the accounting curriculum in the wrong direction (see the discussion in Callahan, 1980, pp. 69–70; Loeb, 1988, p. 321; Geary & Sims, 1994, pp. 3–4, 15–16; Armstrong et al., 2003, p. 10; Bean & Bernardi, 2005, p. 64; Dellaportas et al., 2006, pp. 6–7). In my view, ethics can be taught successfully in colleges and universities and successfully taught to accounting students. The key to providing a meaningful ethics educational experience in an accounting program at a college or university, however, is not designing the program around the goal of changing students' moral behavior, especially in a particular course or a certain set of courses. Rather than attempting to change students' moral behavior, an accounting ethics education program should be designed to promote the seven goals suggested in Table 1 – especially the four essential goals discussed above (see the discussion in Dellaportas et al., 2006, pp. 6–7; also, cf., Geary & Sims, 1994, pp. 3–4, 15–16; Armstrong et al., 2003, p. 10; Van Peursem & Julian, 2006, p. 15). If an accounting ethics educational program, as a minimum, can successfully promote these four essential goals, then, in the long term, students will be more likely to make the right decision when, in practice, they face situations that have ethical dimensions or implications (see the discussion in Armstrong et al., 2003, p. 10; Dellaportas et al., 2006, pp. 6–7; Van Peursem & Julian, 2006, p. 15).[14] In the next section, I discuss the operationalization of goals in teaching ethics to accounting students.

OPERATIONALIZATION OF THE GOALS

In Loeb (1988, pp. 322–324), I provide suggestions on how to operationalize the seven goals that are noted in Table 1 and note that "two key issues" in "the operationalization of these goals are (1) whether accounting ethics should be taught throughout the accounting curriculum or taught in one course ... and (2) what teaching techniques should be used to assist in achieving the goals ..." (p. 322; also see Loeb, 1991, p. 79).

Freestanding Course Versus Integration into the Curriculum

The arguments of whether ethics should be taught in a separate course or integrated into the curriculum have been discussed elsewhere (see, e.g., Fess, 1987, p. 60; Bok, 1988, pp. 7–8; Loeb, 1988, pp. 322–323; 1993, p. 54; 1998,

p. 247; Armstrong, 1993, pp. 79, 88–89; Geary & Sims, 1994, p. 4; Leung & Cooper, 1994, pp. 25–26; 2003–2004 P & E Committee, 2004; Fisher & Swanson, 2005, pp. 13–14).[15] Bok (1988, pp. 7–8) suggests that a professional education curriculum should include both freestanding ethics courses and ethics integrated into other courses (also see Fess, 1987, p. 60). Bok (1988, p. 7) points out that integrating ethics into the curriculum "will make the point that ethics … is relevant to all aspects of professional life."[16] However, Bok (1988, p. 7) also suggests that freestanding ethics courses are needed to provide "in depth" ethics instruction by faculty members who, in turn, can provide academic leadership in ethics education to the discipline. Armstrong (1993, pp. 79, 88–89) suggests the possibility of having two separate ethics courses that surround the integration of ethics in the curriculum. Armstrong (1993, p. 89) refers to such an approach as the "'sandwich approach.'"[17]

Earlier in this paper, in discussing ethics education standards for CPA candidates, I expressed a preference for a freestanding a three semester-hour business ethics course or accounting ethics course. I believe "that the best way" for ethics education to become part of an accounting program's curriculum is to have one freestanding course on business ethics or accounting ethics required within the accounting curriculum (see Loeb, 1998, p. 247; also see, e.g., Fisher & Swanson, 2005). This position may raise concerns such as curriculum space availability, cost, faculty interest, and faculty training in ethics (see Grimstad, 1964, p. 84; May, 1980, pp. 207–208; Fess, 1987, p. 60; Loeb, 1988, pp. 323, 326; 1991, p. 78; 1993, p. 54; Langenderfer & Rockness, 1989, p. 64; Gunz & McCutcheon, 1998, p. 1150; 2003–2004 P & E Committee, 2004). Notwithstanding such concerns, a separate course in business ethics or accounting ethics provides assurance that ethics will be addressed during a student's accounting program (see Loeb, 1998, p. 247). Also, a freestanding course approach, since it generally would involve relatively few faculty members, likely is easier to monitor and change when compared to an integrated approach, which most likely would involve more faculty members (see the discussion in Loeb, 1988, p. 323; 1993, p. 54; 1998, p. 247; Leung & Cooper, 1994, p. 26; cf., 2003–2004 P & E Committee, 2004). Finally, a freestanding course on ethics symbolizes to students and other stakeholders the importance of ethics to the preparation of future accounting professionals and to the practice of accountancy (cf., e.g., Leung & Cooper, 1994, p. 25; Fisher & Swanson, 2005, pp. 13–14; Haas, 2005, p. 68; Shaub, 2006, p. 8).[18]

The University of Maryland, College Park's undergraduate accounting ethics course is not required for graduation as an undergraduate accounting major (see Loeb, 1998, p. 246; Burch & Stevenson, 2005, p. 61). However, the Maryland State Board of Public Accountancy business ethics course

requirement likely results in large numbers of University of Maryland, College Park undergraduate accounting students enrolling in the accounting ethics course. In general, I sense that University of Maryland, College Park undergraduate accounting students now view the accounting ethics course as an integral component of the accounting curriculum. If my sense of the general views of University of Maryland, College Park undergraduate accounting students on the accounting ethics course is correct, then hopefully these students graduate with a sense of the overwhelming cruciality of ethics to the practice of accountancy (cf., e.g., Fisher & Swanson, 2005, pp. 13–14; Haas, 2005, p. 68; Shaub, 2006, p. 8).

Instructional Techniques

A variety of approaches to teaching ethics to accounting students have been discussed in the literature (see, e.g., AAA, 1986, p. 186; Fess, 1987, p. 60; Loeb, 1988, pp. 323–324; 1998, pp. 241–246; Geary & Sims, 1994, pp. 8–10; D'Aquila, 1999, p. 21; IFAC Education Committee, 2003e, pp. 63–64; Van Peursem & Julian, 2006, pp. 21–25).[19] Common techniques that can be used include lecture, case discussion, guest speakers, role-playing, assignment of relevant readings (see, e.g., Fess, 1987, p. 60; Loeb, 1988, pp. 323–324; 1990, pp. 287–289; 1993, p. 55; Beets, 1993; IFAC Education Committee, 2003e, pp. 63–64). Examples of other teaching techniques that have been suggested include students or faculty using existing videotapes (see Loeb, 1990, p. 288; Kerr & Smith, 1995, p. 989), students or faculty preparing ethics related videotapes (see Kerr & Smith, 1995, pp. 989, 991), students presenting a topic or topics in groups/teams (see Loeb, 1998, pp. 243–244; Loeb & Ostas, 2000, p. 232), faculty giving assignments that require student "self-reflection" (Esmond-Kiger & Stein, 1998, see, e.g., p. 219; also see, e.g., IFAC Education Committee, 2003e, p. 64), students studying the stories of accountants who became moral heroes (Knapp et al., 1998; also see Apostolou & Apostolou, 1997), students or faculty using a game (see Haywood et al., 2004), and students or faculty using "fiction or nonfiction" narrative in "oral, written or in cinematic form" (Stewart, 1997, p. 174; also see Kerr & Smith, 1995, pp. 991–992; D'Aquila, 1999, p. 21).

In Loeb (1988, p. 324), I suggest the teaching techniques that an instructor uses to teach accounting ethics should be an individual choice. A faculty member should be "comfortable" with the techniques that he or she chooses to teach accounting ethics (Loeb, 1988, p. 324).[20] On a number of occasions in the past 15 years I have taught accounting ethics in a course that is described in Loeb (1998). While there have been some changes to the course

since Loeb (1998) was published, the essential nature of the course has remained unchanged.

The key methods that I use to teach accounting ethics are "'interactive'" and "'experiential' teaching" (Loeb & Ostas, 2000, p. 226; also see Geary & Sims, 1994, pp. 9, 15; Loeb, 1998, pp. 236, 241–242; IFAC Education Committee, 2003e, pp. 61, 63–64). As part of interactive and experiential teaching, I use case analysis, lectures, role-plays as part of student presentations, and guest speakers (see Loeb, 1998, pp. 239–246). Currently, I also require "a short term paper" and give a "'take home' final examination" (Loeb, 1998, p. 245). My use of most of these techniques is discussed in some detail in Loeb (1998, see especially pp. 242–246). Another possible experiential teaching technique is arranging for a class to visit a prison facility that houses individuals who have been found guilty of business-related offences (see, e.g., Loeb & Ostas, 1997). I have not used this technique with undergraduate accounting ethics classes. However, a discussion of the first time this technique was used in a course, in what is now the Smith School of the University of Maryland, College Park, can be found in Loeb and Ostas (1997).

During recent semesters, a number of guest speakers have made presentations in my accounting ethics class. I have found that guest speakers can bring real-life insights that are related to the role that the guest speaker plays within the accounting profession. For example, when possible, I have arranged for a guest speaker with experience in personnel issues in a public accounting firm to comment on ethics issues and dilemmas relating to personnel matters within a public accounting firm. Also, beginning with the spring 2005 semester, I have been offering extra credit to students who attend all sessions of an ethics-related lecture series offered at the Smith School of the University of Maryland, College Park. The lecture series is scheduled outside of class time.[21]

In general, I have been very satisfied with the techniques that I use to teach the accounting ethics course. I think interactive and experiential education keeps students actively involved with their own learning process and encourages thoughtful class discussion.

INDIVIDUALS TEACHING ACCOUNTING ETHICS

Background of Instructors

Bok (1988, p. 5) indicates that "courses in professional ethics are difficult to teach because they call for preparation in two entirely different

subjects: moral philosophy (or a related discipline) and some practical area of application ...." In contrast, I believe that the individuals who teach a course in accounting ethics should have a background in accounting. Ideally the person should be an accounting faculty member (see Bean & Bernardi, 2005, p. 65). In my 1988 paper (p. 325), I take a similar position (also cf., Loeb, 1990, p. 289). In Loeb (1988, p. 325), I suggest that, except in those instances where an individual is trained in both ethics and accounting, the best approach would be to have accounting ethics taught by a person who had a strong background in accounting and "who has had sufficient training in ethics so that he or she can effectively address goals such as" the seven goals suggested in Loeb (1988, p. 322, Table 1) which are also listed in Table 1 of this current paper.[22]

However, today I now am convinced that formal training in ethics is not necessary to teach accounting ethics. In my view what is necessary is for an accounting faculty member to make a commitment to prepare for and then teach an accounting ethics course. I believe that, for many accounting faculty members, such preparation can be accomplished through a minimum amount of self-study in the ethics literature. With such self-study the faculty member should be ready to teach an accounting ethics course such as I describe in Loeb (1998). Alternatively, I think a similar amount of self-study in ethics would be sufficient for an accounting faculty member to successfully integrate ethics into an accounting course.[23]

The Team Teaching Possibility

On a number of occasions since 1993, I have team-taught a three credit course in business ethics in the University of Maryland, College Park's MBA program and also team-taught business ethics in the University of Maryland College Park's Executive MBA program.[24] Over the years, my team teaching in those courses has been with two different individuals neither of whom was from the accounting discipline. Loeb and Ostas (2000) describes a course that Professor Daniel Ostas and I team-taught in a one evening a week format at various times between 1993 and 1995 (see Loeb & Ostas, 2000, p. 225).

There are reasons for and against the team teaching of ethics that have been discussed elsewhere (see, e.g., The Hastings Center, 1980, pp. 65–66; Callahan, 1980, pp. 79–80; Loeb, 1988, pp. 325–326; 1993, pp. 54–55).[25] Based on my experience, I believe that team teaching a course in accounting ethics, if carefully planned, can be a very effective instructional format. The team teaching of an accounting ethics course can be staffed by two

accounting faculty members or by an accounting member and a faculty member from another discipline who perhaps has a background in ethics (see Loeb, 1988, p. 325; 1993, p. 54). Since team teaching involves interaction and well-planned coordination between the individuals doing the teaching, I suggest limiting team teaching to no more than two individuals. With careful planning, two faculty members team teaching can provide a meaningful education experience for students in an accounting ethics course (see the discussion in Loeb & Ostas, 2000).

DISCUSSION AND CONCLUSIONS

The adoption by the boards of accountancy of Maryland and Texas of an ethics course requirement for CPA candidates, the NASBA current consideration of ethics education as part of the UAA education standards, and IES 1–6 (IFAC Education Committee, 2003a), especially IES 2 (IFAC Education Committee, 2003c) and IES 4 (IFAC Education Committee, 2003e), in the long run, may have a singular effect on ethics education in accounting programs in colleges and universities in the U.S. As suggested earlier, IFAC education standards ultimately may influence the UAA education standards. Further, as noted earlier, NASBA recommendations in the UAA education standards may influence the CPA candidate-related education standards of individual boards of accountancy, and these board of accountancy education standards may influence the accounting curriculum in colleges and universities in the U.S. Thus, the Maryland and Texas ethics education requirements; the NASBA final ethics education standards in the UAA, if those NASBA standards suggest a college or university ethics prerequisite for CPA candidates; and the positive support that IES 1–6, especially IES 2 and IES 4, provide for accounting ethics education, in the long run may result in a significant increase in the demand for ethics education in college and university accounting programs in the U.S.

An increase in the demand for ethics education in accounting programs in colleges and universities in the U.S. likely will encourage a number of accounting faculty members to increase their involvement in ethics education. Accounting faculty may find developing and preparing for an accounting ethics course a time-consuming process. Alternatively, faculty may respond to the possible increased demand for accounting ethics education by integrating ethics into existing courses. One method to accomplish such integration is by adding ethics modules to existing accounting courses (see the discussion in Mantzke, Carnes, & Tolhurst, 2005). Again, accounting

faculty may find integrating ethics into existing courses a time-consuming process. The same would be true for other business faculty if, in response to board of accountancy requirements, ethics is integrated into non-accounting business courses.

As I reflect on my experience in teaching accounting ethics over the last 15 years, I am convinced of the positive value to accounting education of developing and offering a freestanding ethics course to accounting students in colleges and universities. Likewise, if a board of accountancy education standard for CPA candidates permits integration of ethics into the curriculum, and an accounting faculty chooses this approach as a curriculum policy, I also see great value in integrating ethics into the curriculum. As I suggest earlier in this paper, given a choice between the alternatives of a separate course on ethics and integration of ethics into the curriculum, I would personally advocate one freestanding three semester-hour ethics course.

Earlier in this paper, I noted that Bok (1988) argues for both freestanding courses and the integration of ethics into other courses in the curriculum. Also, I previously noted Armstrong's (1993) suggestion of two courses and ethics integrated into the curriculum. However, I think that the current Maryland or Texas ethics education standard of one ethics course is the best approach for a board of accountancy requirement. My personal preference for a freestanding ethics course requirement should not be interpreted that I would discount or reject a CPA candidate-related public policy that would result in colleges and universities providing ethics education either as a freestanding course or integrated into a series of accounting and other business courses. However, I think that one freestanding ethics course will provide more flexibility to a college or university since there likely would be less faculty members needed to teach ethics and changes to the ethics curriculum would be easier to manage (see the discussion in Loeb, 1988, p. 323; 1993, p. 54; Leung & Cooper, 1994, p. 26; cf., 2003–2004 P & E Committee, 2004).

I believe that a faculty member teaching ethics to accounting students should not attempt to indoctrinate students or attempt to change a student's existing behavior – assuming a change is needed.[26] Instead, the goals of teaching ethics to accounting students should be the seven goals suggested in Table 1 or alternatively the four of those seven goals that earlier I suggest are essential. Ultimately, accounting ethics education should prepare accounting students to recognize ethical issues and to properly address the uncertainties and ethical dilemmas that may arise in practice.[27]

My many years of teaching an accounting ethics course suggests that the use of interactive and experiential education is the best way to approach the

development of an accounting ethics course or portions of course(s) if ethics is integrated into the curriculum (see the discussion in Loeb, 1998). I believe that an accounting ethics education should be designed to excite accounting students about the study of ethics. A purely lecture format may have the opposite effect and result frustration to both the instructor and the students (cf., Bok & Callahan, 1979, p. 32).

A board of accountancy requirement mandating an ethics course or ethics integrated into a number of courses as a prerequisite to taking the CPA examination places pressure on colleges and universities to respond to the requirement. I sense that historically the CPA examination has had an influence on the accounting education (see the discussion in Langenderfer & Rockness, 1989, pp. 63–64; Reckers, 2006). However, two key benefits of a board of accountancy ethics education requirement are (1) the preparation that such a requirement can provide students for the practice of accounting and (2) the message that such a requirement sends to students and other stakeholders about the cruciality of ethics to the practice of accountancy (cf., e.g., Fisher & Swanson, 2005, pp. 13–14; Haas, 2005, p. 68; Shaub, 2006, p. 8).

An ethics course based on the seven goals suggested in Table 1 or the four essential goals discussed earlier can provide students with the knowledge and skills to face the complex and difficult issues that can arise in the practice of accountancy. Also, the existence of a required ethics course in a college or university accounting curriculum may suggest to students that ethics is of equal importance with the other courses that students take during their college or university accounting education (see Haas, 2005, p. 68; cf., e.g., Leung & Cooper, 1994, p. 25; Fisher & Swanson, 2005, pp. 13–14; Shaub, 2006, p. 8). Thus, I believe that public policy makers in Maryland and Texas, by requiring an ethics course, are moving accounting education in the appropriate direction in preparing students for the practice of accountancy in the 21st century.

NOTES

1. Over the years the AAA P & E Committee has been involved in a number of activities. I further discuss some of the activities of the AAA P & E Committee later in the paper. Also, the original name of this committee was "Advisory Committee on Professionalism and Ethics" Langenderfer (1990, p. i). In this paper, I will use the committee's current name (Professionalism and Ethics Committee).

2. In 1993, I began team teaching a graduate course in business ethics in now what is the Robert H. Smith School of Business (Smith School) of the University of Maryland,

College Park (see, e.g., the discussion in Loeb & Ostas, 2000). In 1996, what is now the Smith School began offering a business ethics experiential learning module (ELM) to its full-time MBA students and in 1997 a business ethics ELM to its part-time MBA students. I have coordinated these ELMs (see Loeb & Ostas, 1997, especially pp. 21–22, including n. 1; 2000, pp. 225–226, n. 1). In more recent years, I have also team-taught an ethics course in the Smith School's Executive MBA program.

3. As discussed later in my paper, a letter (2003–2004 P & E Committee, 2004) was prepared by a past AAA P & E Committee (the 2003–2004 Committee) and sent by the AAA to the National Association of State Boards of Accountancy.

4. See Reckers (2006, pp. 32–33) for a discussion of the UAA. The intensive ethics requirements were not the only curriculum suggestions in the exposure draft (see, e.g., NASBA, 2005; Rayburn, 2006, p. 1; Reckers, 2006, pp. 33–34).

5. At the time of this writing, these comments can be found at NASBA (2006c). Also, see Reckers (2006, pp. 35–37) for a discussion of some of the concerns with the NASBA exposure draft.

6. Reckers (2006, p. 33) suggests that "most" boards of accountancy can make changes to be in conformity with revised NASBA education standards for CPA candidates without legislation by the relevant legislative body in the jurisdiction. However, Reckers (2006, pp. 39–40) suggests that, if a board of accountancy wishes to make such changes in education standards, those changes are subject to "oversight" by the relevant legislative body in the jurisdiction. In the remainder of this paper, I will assume that boards of accountancy, wishing to adopt revised NASBA education standards, do so by working within the relevant public policy framework of their jurisdictions.

7. At the time of this writing, comments on NASBA Education Task Force (2006) can be found at NASBA (2006b). NASBA (2006b) suggests the task force will be seeking additional input.

8. The IFAC Education Committee is now called the "International Accounting Education Standards Board" (IFAC, 2006b).

9. As noted earlier in my paper, Dellaportas et al. (2006, p. 5) discuss the issue of the mandatory character of the IESs and my discussion of that issue follows their discussion. My comments in the next two sentences of this note follow the discussion in Dellaportas et al. (2006, pp. 5, 9). More specifically, IFAC Education Committee (2003h, p. 3) in paragraph 6 suggests that in a particular nation factors such as "culture," "language," and what an accountant does may affect how a member organization reacts to an IES. Further, paragraph 6 of IFAC Education Committee (2003h, p. 3) indicates that the IESs provide "the essential elements" and the member organizations should provide the "detailed" educational specifics needed for qualification. Additionally, IFAC Education Committee (2003h, p. 6) in paragraphs 17 and 18 further differentiates the significance of the wording in IESs. More specifically matters discussed in "bold type-face" are considered standards and the remaining exposition is considered "commentary" (paragraph 17). Member organizations only need to comply with material in bold type-face (Paragraph 17). Also, see IFAC Education Committee (2003i, p. 26). Also, in this paper, I refer to more than one IEG or IEP as IEGs or IEPs respectively.

10. At this writing, there are indications that an IEG relating to IES 4 is in development (see, e.g., IFAC, 2006c; Leung & Cooper, 2006, p. 2; Dellaportas et al., 2006, p. 10).

11. Also, see the discussion in Bernardi et al. (2005).

12. See Loeb (1988, p. 326) for a discussion, which includes comments from relevant literature, on how teaching ethics and conducting ethics research can affect the career of a faculty member (including an accounting faculty member). Also, see Loeb (1993, p. 55) and Gunz and McCutcheon (1998, p. 1150).

13. See Loeb (1988, pp. 317–319) for a discussion, which includes comments from relevant literature, on the need for ethics education in accounting.

14. Geary and Sims (1994, p. 4) suggest a number of factors that they feel are needed for "effective ethics education" including "agreement about the broader goals of ethics education in accounting." Also, Loeb (1988, p. 321) provides comments from relevant literature to support Callahan's (1980, pp. 69–70) idea of preparing students for change rather than attempting to change their moral behavior. Additionally, see Loeb (1988, p. 320) for a discussion, which includes comments from relevant literature, of some of the goals for ethics education suggested in Callahan (1980). Also see Loeb (1993, pp. 53–54).

15. Loeb (1988, pp. 322–323) reviews a number of works that comment on the issue of a freestanding ethics course versus the integration of ethics into the curriculum (also see, Loeb, 1993, p. 54). Also see IES 4, paragraph 17 (IFAC Education Committee, 2003e, p. 63) where the discussion is in terms of "subject" not course. Also see IES 4, paragraph 18 (IFAC Education Committee, 2003e, p. 63).

16. Cf., IES 4, paragraph 18 (IFAC Education Committee, 2003e, p. 63).

17. IES 4 in paragraphs 17 and 18 provides support for use of both approaches – a freestanding ethics course and integration of ethics into the curriculum (IFAC Education Committee, 2003e, p. 63). Further IES 4 in paragraph 17 seems to suggest that both approaches can be used in the same educational program (IFAC Education Committee, 2003e, p. 63).

18. In Loeb (1993, p. 56), I suggest that it might be preferable for a discipline beginning an ethics education movement to emphasize integrating ethics into the curriculum rather than having a separate ethics course. This is the opposite of my current position. Also, see the discussion in 2003–2004 P & E Committee (2004).

19. Some other examples of the literature discussing approaches to teaching ethics to accounting students are included below in the text of my paper. Also, Loeb (1988, pp. 323–324) provides a literature review and discussion of the issue of instructional techniques that can be used to teach ethics.

20. In Loeb (1988, p. 324), I support this view with a comment from and references to relevant literature.

21. I view my use of guest speakers and the ethics lecture series as interactive learning since I encourage the guest speakers to include a question and answer component in their presentation. Also, some colleagues in the Smith School of the University of Maryland, College Park who teach another section or sections of this ethics course or other courses, depending on the semester, offer extra credit to students for attending session(s) of the ethics lecture series. Sometimes one or more Smith School colleague(s), depending on the semester, encourage students to attend session(s) of the ethics lecture series. Also, see the discussion of the use of guest speakers in Loeb (1990, pp. 287–288) (including a comment from relevant literature) and (Loeb & Ostas, 2000, p. 231).

22. See Loeb (1988, pp. 324–325) for a discussion, which includes comments from relevant literature, on the issue of what background instructors should have to teach ethics to accounting students. Also, see Loeb (1993, p. 54).

23. I believe that the reading and study of portions of one or more business ethics textbooks may provide for many accounting faculty members sufficient background to successfully teach an accounting ethics course or integrate ethics into an accounting course.

24. Also, I have been coordinator of the business ethics ELMs since the ELMs began. There have been a large number of students each year taking the business ethics ELMs and the educational program required the involvement of more than one faculty member. I always have had an associate coordinator and over the years three individuals at different times have been associate coordinator. Also, each year, in addition to the associate coordinator, I have involved a number of faculty members in the operation of the business ethics ELMs (see the discussion in Loeb & Ostas, 1997). Also see Note 2.

25. See Loeb (1988, pp. 325–326) for a discussion, which includes comments from relevant literature, on the advantages and disadvantages of team teaching ethics. Also, see Loeb and Ostas (2000, p. 225; also pp. 234–235, which include comments from relevant literature).

26. The issue of indoctrination is discussed in Huss and Patterson (1993, see especially pp. 239–240, 242). Also see the discussion in Callahan (1980, pp. 69, 71–72) and Loeb (1991, p. 78).

27. See the discussion of the ideas reflected in this statement earlier in my paper which update Loeb (1998, pp. 238, 249, n. 6).

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AUTHOR'S ADDENDUM

While my paper was in production, the following work was published: International Accounting Education Standards Board, (Project Team: P. Leung, Project Leader; B. J. Cooper; S. Dellaportas; B. Jackling; & H. Leslie), (August 2006), *Approaches to the Development and Maintenance of Professional Values, Ethics and Attitudes in Accounting Education Programs*, Information Paper, New York: International Federation of Accountants, http://www.ifac.org/Store/Details.tmpl?SID = 1155152665859443 &Cart = 115688794575018. Consequently, except for my comments in the next sentence, my article has no other reference to that new International Federation of Accountants (IFAC) publication. Among other things, in the Foreword the new IFAC publication suggests that IEGs and IEPs have been re-titled and then later that publication provides additional comments on the mandatory nature of IESs.

LOEB'S CONTRIBUTION TO ACCOUNTING ETHICS EDUCATION AND RESEARCH

Steven M. Mintz

ABSTRACT

Almost 20 years has passed since Loeb (1988) described the goals of accounting ethics education. During that time, accounting ethics researchers have explored how best to enhance students' ethical reasoning skills and moral judgment. The objective is to "set the stage" for a change in ethical behavior if not facilitate an actual change.

The motivation for change has developed over time in response to concerns about accountants' ethics and auditor decision making that has been caused by nothing less than a change in culture in the accounting profession. The support to enable change arises from moral philosophy, virtue ethics, and the existence of principles of behavior in the AICPA Code of Professional Conduct (Code) (American Institute of Certified Public Accountants, AICPA, 1997).

The recent scandals have made it clear that now is the time to get serious about accounting ethics education. The debate of whether ethics should be taught is moot. We teach ethics by not teaching ethics. The argument that you cannot teach ethics is irrelevant. We can teach it; students may choose not to learn it. As Loeb pointed out years ago, ethics is not viewed as a primary area of accounting teaching and research and that neglect is a risky career strategy.

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LOEB'S CONTRIBUTION TO ACCOUNTING ETHICS EDUCATION AND RESEARCH

Steve Loeb has published a variety of papers in accounting ethics. One of the most significant papers for accounting ethics research and education is: "*Teaching students accounting ethics: Some crucial issues*." In that paper, Loeb (1988) describes the goals of accounting ethics education. The goals have guided accounting ethics researchers for years and take on a new meaning in the aftermath of the recent accounting scandals and passage of the Sarbanes–Oxley Act of 2002 (SOX). The purpose of this paper is to revisit Loeb's goals and link them to specific research that has been, at least in the author's view, motivated either directly or indirectly by Loeb' paper.

Loeb's (1988, p.322) goals include seven items drawn from earlier research on "Goals in the teaching of ethics by Daniel Callahan (1980)."

1. Relate accounting education to moral issues.
2. Recognize issues in accounting that have ethical implications.
3. Develop 'a sense of moral obligation' or responsibility.
4. Develop the abilities needed to deal with ethical conflicts or dilemmas.
5. Learn to deal with the uncertainties of the accounting profession.
6. 'Set the stage for' a change in ethical behavior.
7. Appreciate and understand the history and composition of all aspects of accounting ethics and their relationship to the general field of ethics.

RELATE ACCOUNTING EDUCATION TO MORAL ISSUES

In 1988, the American Accounting Association established a Professionalism and Ethics Committee that led the way in early efforts to sensitize educators to the ethical issues faced by accounting professionals in the context of broader moral issues. The Professionalism and Ethics Committee conducted a series of seminars to train faculty to use philosophical reasoning methods and apply a case study approach to evaluate ethical dilemmas faced by accounting professionals. The author attended a few of these sessions and found them to be invaluable in developing an early-stage learning framework to teach ethics better to accounting students. Ironically, it was Arthur Andersen that held other workshops in the name of the accounting profession that were more comprehensive and immersed participants in the application of ethical reasoning in the classroom.

Research in Moral Development

Kohlberg (1964) theory of "cognitive development" postulates that moral development occurs in a specific sequence of six stages that may be divided into three levels of moral reasoning – preconventional, conventional, and postconventional. Higher levels lead to increased abilities to reason morally. Armstrong (1987) was one of the first educators to discuss moral development and accounting education. Armstrong studied whether accounting students could learn to reason at a higher level as reflected in pre-and-post tests of moral reasoning. The Defining Issues Test (DIT) that Rest (1994) used in a variety of studies serves as the tool to measure a students' ability to reason ethically (*P*-score). Armstrong's own teaching experiences and DIT measurements led her to conclude that ethics education can raise a student's DIT score.

A variety of early researchers measured students' ability to reason ethically including St. Pierre, Nelson, and Gabbin (1990), Ponemon (1990, 1992), Ponemon and Glazer (1990), Jeffrey (1993), Shaub (1994), and Bernardi (1995). Other researchers linked ethical reasoning to auditors' ability to make ethical judgments (Ponemon & Gabhart, 1990, 1994; Lampe and Finn, 1992; Shaub, 1994). This represents a major advance in accounting ethics research since if we, as accounting educators, are not able to influence our students' ability to be more ethical in carrying out professional obligations, then what is the point of teaching ethics? Shaub (1994, p. 22) may have summed it up best when he said: "A higher DIT score may indicate a higher cognitive, or logical, capacity. For auditors, this would reflect itself in superior performance on standard audit tasks."

Early studies indicated that the mean DIT P-score for accounting students were below the norm for all college students suggesting the nature of the student who majors in accounting reasons below the norm (Ponemon, 1993; Ponemon & Glazer, 1990; Shaub, 1994). However, other research has shown that accounting students reason above the norm (Armstrong, 1993; Jeffrey, 1993).

Implications for Accounting Education

A popular technique to teach ethics and raise the moral reasoning abilities of accounting students is the case method. Langenderfer and Rockness (1989) made important contributions in providing a useful framework to teach ethics using case studies. They provide an eight-step approach to teaching ethical decision making that is consistent with Kohlberg's stages of moral development.

Armstrong (1993) suggests a "sandwich" approach to teach ethics to accounting students. She recommends that a philosophy of ethics course should introduce moral issues, followed by integration throughout the accounting curriculum, and the accounting program should include a separate course in accounting ethics.

Loeb (1990) believes that whistleblowing is an important topic in accounting education. He identifies four learning goals of teaching whistleblowing that emphasize understanding whistleblowing and learning approaches to deal with it. Finn (1995) develops an employee-organization whistleblowing model that emphasizes the need for a strong internal organization environment. Sack (1990) cautions firms to be aware of subtle cultural aspects of the organization that may imply that firm policies are more window dressing than reflecting actual practice. He cites the example of penalizing employees for standing up to the client as sending a message that is more powerful than any written firm policy on independence. Sack's insights bear directly on the whistleblower-defense provisions recognized in the SOX.

RECOGNIZE ISSUES IN ACCOUNTING THAT HAVE ETHICAL IMPLICATIONS

Gaa was one of the earliest educators to meaningfully link moral reasoning with ethical dilemmas faced by accountants and auditors. Gaa's research sheds light on the moral responsibilities of auditors in meeting their societal obligations. Gaa published two papers that explored regulation of auditors by the government (1991) and philosophical and psychological aspects of the auditors' role Gaa, (1992). In the former paper, Gaa (1991) analyzed the effectiveness of auditor regulation, while in the latter paper (1993, pp. 15–22) he presented a thoughtful discussion of how auditors should make decisions with respect to responsibilities to the public interest. Gaa suggests that auditors should follow a "moral point of view." Essentially, the idea is for auditors to be willing to put the public interest ahead of others interests including the client's interest and their self-interest. Gaa's words ring loud and clear in the aftermath of the scandals at Enron, WorldCom, and many other companies.

Mintz (1995) points out that ethical conflict in accounting occurs when accountants perceive that their duties toward one group are inconsistent with their duties and responsibilities toward some other group or their own self-interests. The existence of a moral point of view in accounting implies that more research is needed to develop an approach to accomplish the challenging task.

DEVELOPING A SENSE OF MORAL OBLIGATION OR RESPONSIBILITY

Focault (1986) believes that moral behavior consists of the actual behavior of individuals in relation to their moral code. The question is whether individuals comply more or less fully with a standard of conduct, in what manner they obey or resist an interdiction or a prescription, and in what manner they respect or disregard a set of values. According to Rajchman (1986), ethics is distinguished from moral behavior and the moral code because ethics concerns the manner in which a person ought to conduct him or herself in order to become the right kind of person.

Focault (1986) argues that the ethical aspects of morality have not been sufficiently studied. He divides ethics into four subparts: ethical substance, mode of subjection, self-forming activity, and telos. Ethical substance refers to those aspects of behavior subject to moral judgment not just technical judgment or opinion. For example, Baker (1996) points out that a CPA's independence is subject to moral judgment and has ethical substance, whereas the CPA's ability to prepare a spreadsheet properly is a matter of technical judgment. Focault (1986) points out that the mode of subjection is the way in which a person is motivated to recognize their moral obligations. While CPAs are required to adhere to a strict code of professional conduct, some fail to internalize the unwritten rules about how one should behave toward clients. Baker (1996) notes the "lack of moral focus" appears to associate with increasing pressures placed on CPAs.

The nature of the self-forming activity that changes someone or adds to the ethical base is critical to meet Loeb's goal to set the stage for a change in behavior. The process can vary from self-examination to the selection-socialization process postulated by Ponemon (1992). Selection-socialization theory suggests that auditors who are unable to conform to ethical norms or values of the firm's management are "weeded out." Lampe and Finn (1992) and Lampe (1994) suggest that accountants may self-select into a rule-based profession in which deviation from the rules is discouraged. If these researchers are correct, it may be difficult to set the stage for a change in ethical behavior, which Loeb (1988) notes the long term nature of that objective and challenges in meeting the goal.

Baker (1977, 1993) points out that the telos of public accounting is to develop the ideal partner who is an ethical being not in the sense of conforming to the code of conduct, but in being able to satisfy clients, bringing in new business, and be technically astute, all while simultaneously giving the impression of acting in the highest ethical manner. Baker (1996, p. 81) notes

that while most contemporary moral philosophy focuses on discussions and elaborations of moral codes "Virtually nothing concerning a person's relationship to him or herself is thought to be relevant to studies of ethics." The implications of these statements for accounting ethics education and research are substantial. Without one's strong ethical sense of self, it is unlikely that our current students will be able to resist the pressures to put aside their ethics for the sake of client harmony or growth of the CPA firm's client base.

DEVELOP THE ABILITIES NEEDED TO DEAL WITH ETHICAL CONFLICT AND THE UNCERTAINTIES IN ACCOUNTING

The fourth and fifth goals of accounting ethics education are critical to success of the effort. The same skills that help to deal with ethical conflict facilitate coping with uncertainty in accounting with respect to situations when the rules are unclear. Accounting professionals need to develop ethical judgment to successfully (morally) resolve ethical dilemmas that develop in these situations. Ethical judgment is necessary when conditions are insufficient and ensure by taking ethical action , for example, top management imposes pressure on an internal accountants or the external auditors to go along with false and misleading financial statement information. Accounting ethics researchers, recently have shifted gears from early studies of ethical reasoning and developing judgment skills to identifying the attributes needed to take moral action. Rest's (1994) model provides the framework for studying four components that enable a decision maker to take moral action. These include: moral sensitivity, moral judgment, moral motivation, and moral character.

Moral Sensitivity and Moral Judgment

Moral sensitivity relates to the degree of awareness of how one's actions affect other people. Cohen, Pant, and Sharp (1995a, 1995b, 1996, 2001) use Reidenbach and Robin's (1988) Multidimensional Ethics Scale (MES) to investigate the association between ethical orientation and auditors' ethical sensitivity. Ethical orientation represents the degree to which various ethical principles such as, utilitarianism, justice and fairness, duties and obligations, cultural acceptance (relativism), and self-interest, are used to judge ethical situations. As Jones (2003) points out, in contrast to the stable and structured view of ethical development advanced by Kohlberg and Turiel (1976),

ethical orientation is situation-specific. Although there was considerable variation among the approaches used to judge the vignettes in their studies, Cohen et al. (1995a, 1995b, 1996, 2001) found that auditors tend to define ethical/unethical acts (ethical orientation) based upon utilitarianism, justice/fairness, and duties/obligations.

Moral judgment enables an individual to evaluate the moral justification for alternative courses of action generated from the first component. Abdolmohammadi (2002) points out that attributes such as competence and experience can be important elements of moral sensitivity, while decisiveness may help with the second.

Shaub, Finn, and Munter (1993, pp. 145–149) use a path analytic approach to examine the relationship among ethical sensitivity, ethical orientation, professional commitment, and organizational commitment. They found that ethical orientation, but not professional or organizational commitment, influences ethical sensitivity. Their results suggest that auditors' cultural environment and individual experiences influence ethical sensitivity rather than rules of conduct. Since one's individual experiences and the environment surrounding one's experiences changes over time, it is reasonable to conclude that Loeb's seventh goal of setting the stage for a change in ethical behavior will be significantly affected by those experiences and events.

Moral Motivation

Rest's third component, moral motivation, has the comparative importance assigned by the individual to moral values (e.g., lack of interest in falsifying expense reports) other than self-interest values that might include maximization of one's own wealth whatever the costs. Abdolmohammadi (2002) develops an inventory of attributes for ethical decision making that includes, in order of importance, honesty, conscientiousness, objectivity (impartiality), trustworthiness, fairness, compliance with rules of conduct, professional skepticism, and compliance with auditing standards. The inclusion of professional skepticism is noteworthy because of the increased focus placed on identifying fraud risks in statement *on Auditing Standards (SAS) No. 99* (AICPA, 2002).

Shaub and Lawrence (2002) point out that the Securities and Exchange Commission has cited a lack of professional skepticism as one of the most serious auditing-related problems in their enforcement actions against CPA firms, yet no serious attempt has been made by firms to measure professional skepticism. They create a taxonomy of professional skepticism that measures skeptics, aggressive skeptics, reluctant skeptics, or conflicted skeptics

according to their tendencies to think and act skeptically. In a separate paper, Shaub (2004) develops a model of trust, independence, and professional skepticism.

Virtue

The final component of Rest's model is moral character. It "involves ego strength, perseverance, backbone, toughness, strength of conviction, and courage" (Rest, 1994, p. 24) for moral behavior. Mintz (1995) identifies other moral attributes to carry out moral behavior including integrity, reliability, and dependability. He believes virtue theory supports developing these traits of character.

Virtue dates back to the ancient Greek philosophers, especially Plato and Aristotle. In writing about Aristotle's account of the virtues, MacIntyre (1984, pp. 149–150) states that the exercise of virtue requires "a capacity to judge and do the right thing in the right place at the right time in the right way." Judgment is exercised not through a routinizable application of rules, but by possessing those dispositions, which enable the proper ("right") choices to be made.

Pincoffs (1986, pp. 75–84) believes that virtues (and vices) are dispositional properties that provide grounds for preference (or avoidance) of persons. He divides virtues into two categories – instrumental and noninstrumental. The instrumental virtues enable a person to successfully achieve goals. Mintz (1995, p. 253) points out that these are positive traits of character for an independent auditor because their presence enables the auditor to complete the engagement with due care and the integrity needed to fight off client pressures. The noninstrumental virtues relate more to doing tasks well and include trustworthiness, an essential characteristic for a CPA in the eyes of a client and the public.

Auditor Ethical Judgment

Falk (1995) describes the four basic attributes of virtue ethics theory including the notion of virtue, ethical judgment, nurturing community, and moral exemplars. The first two attributes are concerned with the personal dimension of ethical decision making. Solomon (1993) points out that the second two attributes are concerned with the community from which an individual's definition of virtue is based. Dobson and Armstrong (1995) and Thorne (1998) maintain that it is the personal dimension of virtue-ethics theory that identifies the importance of virtue to individuals' and to auditors'

ethical judgment. Libby and Thorne (2004) note that a virtuous auditor is one, who despite with personal consequences satisfies his/her professional obligation which may include the loss of a client to fulfill one's ethical duties. Libby and Thorne (2004) build on Pincoff's instrumental and non-instrumental virtues to develop an inventory of 55 auditors' virtues and organize them according to a typology that distinguishes the underlying dimensions of the auditors' virtue construct. They found that auditors perceive four specific virtues as critically important including being independent, objective, truthful, and having integrity.

Decision making for auditors occurs within the context of the culture of an accounting firm. Some researchers suggest the existence of an inverse relationship (inverted U) between level of moral reasoning and position level within the firm (Ponemon, 1990, 1992) and (Shaub, 1994). Ponemon and Shaub hypothesize that the older partners had a different educational experience relative to the new partners. However, it would take a longitudinal study to differentiate. Bernardi and Arnold's (2004) longitudinal study does not show the inverted U.

"SET THE STAGE" FOR A CHANGE IN ETHICAL BEHAVIOR

Armstrong (1987) made a prophetic statement with respect to Congressional investigations following the rash of accounting scandals in the early 1980s and the reawakening in the academy to the need for business ethics education. She said: "Once again the pendulum has returned and professional ethics are in the spotlight." Twenty years later the accounting profession is still trying to explain how and why accountants and auditors at companies such as Enron, WorldCom, Tyco, and Adelphia failed to exercise the moral courage expected by the public and incorporated as an ethical obligation in the integrity standard of the AICPA (1997) Code of Professional Conduct.

Ethics in the Business School Curriculum

The American Assembly of Collegiate Schools of Business (AACSB) adopted in 2003 curriculum standards (AACSB, 2004) to guide degree programs that include learning experiences in general knowledge and skill areas including "ethical understanding and reasoning abilities." In 2004, the AACSB established a task force to examine ways of strengthening management education in the aftermath of the business failures. The task force

issued a report (AACSB, 2004) encouraging "administrators and faculty in business education to contemplate their current approaches to ethics education and to explore methods to strengthen this vital part of the curriculum." AACSB identifies three areas that should receive meaningful coverage in business ethics education: ethical leadership, ethical decision-making, and corporate governance.

Curriculum coverage of ethical decision making has been an important theme in ethics education in business schools, since the late 1980s. The implication is that more needs to be done in the areas of ethical leadership and corporate governance. Accounting ethics researchers should heed the call because ethical leaders are needed in accounting to ensure governance provisions are complied with as required in SOX.

Wyatt (2004, pp. 50–51) discusses the need to reestablish professionalism following the recent accounting scandals. He notes the importance of changing the tone at the top of accounting firms. Sadly, the Treadway Commission Report (1987) recommended the same with respect to top management in public companies. The Commission of Sponsoring Organizations (COSO) issued a report to emphasize the importance of the tone at the top and to create an ethical culture in an organization. A skeptic might believe that perhaps the accounting firms did not think about the recommendation applied to them.

Jennings (2004) raises an important question for consideration: "When all the reform dust settles … and the new statutes, regulations, and rules are implemented, auditors and those who educate them will still be left with the same question: why were auditors willing to allow the types of financial reports and reporting decisions that produced fundamentally unfair and inaccurate portraits of the companies they were auditing?" Jennings (2004, p. 8) suggests that a change is needed to move ethics education in business schools away from focusing on broad-based social responsibility to using six seminal works on ethics and decision making to help students understand the realities and pressures of ethical crossroads. She describes the six writings that can help accountants, auditors and managers to refocus on making better ethical choices at critical junctures. Jennings approach provides a direct link in helping to create a change in ethical behavior.

Gaa and Thorne (2004, p. 2) in their introduction to a special *Issues in Accounting Education* on professionalism and ethics in accounting education, point out that accounting ethics education has focused on developing the competencies required of accountants in order to act ethically. They suggest that the coverage of a choice dimension rather than personal and professional values and virtue has been imbalanced. The theory of virtue has

particular importance in accounting because it is an agent-based approach to making moral decisions. Rather than focusing attention only on the action, virtue ethics emphasizes the qualities of one's character that enable an individual to internalize the values that lead to making a moral choice.

Waddock (2005, pp. 146–147) contends that until business schools teach future accountants and leaders how deep the connections are between business, society, nature, and the world, corporations will continue to be run by hollow leaders who have no sense of ethics or responsibility. She calls for a "mindful accounting education" that emphasizes fulfilling of ethical duties. Similarly, Copeland (2005, p. 36) emphasizes the teaching of ethics to accounting students as an imperative to deal with the "ethical breakdown" not only in business but also in society. He challenges "the academic community to play an important role in the reconstruction of the accounting and auditing profession because of their dual roles as instructors and researchers."

One positive result of SOX for accounting ethics education is the focus being placed on identifying the myriad of resources available today to teach ethics to accounting students. Thomas (2004) develops a 'Post-Enron' annotated bibliography of resources for accounting professors who want to either design a stand-alone course in accounting ethics or who wish to integrate a significant component of ethics into traditional courses across the curriculum. Thomas includes classics, such as the works by Kohlberg and Rest, and more recent publications including "*Celebrating Accounting Heroes: An Alternative Approach to Teaching Ethics*" by Knapp (2006).

Does anyone doubt that the accounting profession, at least in recent years, lacks moral role models to use in classroom instruction? One exception is Cynthia Cooper, the former vice president of the internal audit department at WorldCom. Cooper directed an exhaustive internal audit that uncovered the extent of the fraud. She brought it to the attention of the board of directors and it acted swiftly to fire the former CFO, Scott Sullivan, who had directed the accounting fraud. Cooper was named a 2002 Time Magazine Person of the Year. In 2003, she received the Accounting Exemplar Award of the American Accounting Association for her notable contribution to professionalism and ethics in accounting practice. The AICPA inducted her into its Hall of Fame in 2004, the first woman to receive that honor.

WHERE DO WE GO FROM HERE?

Loeb's (1988) last goal is to appreciate and understand the history and composition of all aspects of accounting ethics and their relationship to the

general field of ethics. The essential elements of this goal have already been addressed. The painful conclusion is that the chief financial officers who created the structured financial transactions that triggered fraud and those who went along with management during the fraud had no sense of history or accounting ethics. They repeated past mistakes made in the frauds of the 1980s (i.e., ZZZZ Best; ESM Government Securities; and the savings and loan debacle). They ignored prior calls for corporations to establish an ethical tone at the top (COSO, 1992). They ignored the lessons of the past.

We need to recommit to accounting ethics education. We must do this not because AACSB recommends it, or because the National Association of State Boards of Accountancy (NASBA, 2006) issued a framework for accounting ethics education that might lead to enhanced coverage of ethics. We need to engage accounting students in meaningful ethics instruction because next time also we (accounting educators) will be blamed if our current graduates continue the dubious tradition in accounting of standing silently by or enabling financial statement fraud to occur.

Many of us teach in state colleges and universities where a student's education is publicly funded. The public has a right to demand that we get serious about teaching ethics to accounting students. We are, after all, training future business leaders. It is questionable whether society will tolerate another wave of accounting scandals. Remember, the books do not get cooked unless accountants and auditors sanction that result.

What will it take to get the job done? First, we have to move beyond the debate whether ethics can be taught. We can teach it, although students may choose not to learn it. We can also teach about leases and pensions, and students might choose to tune us out on those issues as well. Moreover, we teach ethics by not teaching ethics. When we ignore having discussions on ethics with accounting students, we send the message that ethics considerations are not relevant to curriculum coverage in financial reporting, management decision making, taxation, and auditing. But, how can that be when three professional associations have separate codes of ethics and ethical standards defining professional practice. These include the American Institute of CPAs, the Institute of Management Accountants, and the Institute of Internal Auditors (internal auditing).

We do not need more legislation or regulation. The effort to teach ethics to accounting students should be seen as an obligation of being accounting educators. We do need the support of deans, and that is where the AACSB has a role to play. The AASCB's "hands-off" approach to identifying specific curriculum standards and courses has not worked very well with respect to a meaningful business school ethics education that helps future business

leaders to counteract the pressures in the workplace to compromise one's values in the name of "making the numbers." The AACSB needs to move quickly to require business and/or discipline-specific ethics courses for all accredited colleges and universities. Even though the Association has drifted away from dictating any specific curriculum coverage in recent years, the teaching of ethics should be an exception because of the potential costs to society if we have to go through another massive wave of business failures formed by accounting neglect of ethical obligations.

We also need the support of those business schools that offer a PhD in accounting. It is unconscionable that these institutions still do not make it a major mandate for all accounting doctoral graduates to be well-schooled in how to teach accounting ethics. We fail ourselves by doing nothing less. Perhaps the Federation of Schools of Accountancy can take the lead in this regard. Loeb (1988, p. 326) warned years ago that ethics was not viewed as a primary area of accounting teaching and research and that the neglect was a risky career strategy.

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THE GROWTH OF ACCOUNTING RESEARCH IN ETHICS JOURNALS: A 45-YEAR STUDY

Richard A. Bernardi and David F. Bean

ABSTRACT

The purpose of this research is to chronicle the increased level of accounting research published in ethics journals over the 45-year period from 1960 through 2004.[1] *This is an especially timely piece of research as we celebrate two distinctive events in 2005 – 10th Symposium on Ethics Research in Accounting and 10th volume of Research on Accounting Ethics (hereafter referred to as Research on Professional Responsibility and Ethics in Accounting). While this is a "10th-anniversary year", our heritage in ethics research dates back to the first accounting scholar published in Business & Society in 1969. The following period witnessed a dramatic increase in the level of research published in ethics journals by accounting doctorates. The data indicate that both the publication of Research on Professional Responsibility and Ethics in Accounting and our annual Ethics Symposium have increased the level of published ethics research in accounting.*

Recently, the accounting profession has been embarrassed by scandals at Enron and WorldCom and the demise of one of its "Big-5" accounting firms. However, these are not the only scandals that have embarrassed the profession; other examples are readily available. The accounting profession has taken on the aura of a marketer of services rather than that of a profession dedicated

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and obligated to service society. The profession ignored the warnings of individuals such as Abe Briloff who foresaw the eventual collapse in public confidence in the accounting profession. Even before the Enron-Arthur Andersen crisis, there is an increasing body of evidence that supports concerns about the declining independence and objectivity of auditors (O'Connell, 2001).

The challenges to our academy are to do more relevant research and to "instill moral values in our students [and that] technical proficiency is not enough" (Fuerman, 2004, p. 912). This study documents our journey toward meeting these challenges by chronicling the increased level of ethics research in accounting that continues the work of early proponents on professional transparency. The current research examines publications in ethics journals over the 45-year period 1960 through 2004. As part of this study, we test whether the advent of the Ethics Symposium and/or the publication of *Research on Professional Responsibility and Ethics in Accounting* increased the level of published research in accounting ethics.

THE PROCESS OF LAUNCHING A NEW JOURNAL

Bailey (1989) provides an insight into the decision process that proposed journals navigate prior to being published; she uses Elsevier as a case study in this research. She indicates that the primary reasons for a new journal include: (1) a researcher who perceives a need approaches the publisher and offers to be the editor; (2) scientific societies that do not have the means to publish their own journal but have a large author base; and (3) the publisher's editorial staff identifies an unfilled need. If one considers the evolution of *Research on Professional Responsibility and Ethics in Accounting* (formerly *Research on Accounting Ethics*), the time frame included our first ethics conference held in Binghamton, New York, that demonstrated the potential for an unfilled need. Shortly after this conference, Ponemon approached JAI Press, which was purchased by Elsevier, with the concept of a new journal devoted to accounting ethics describing it as a "boutique journal" to the lead author. Ponemon was the editor for volumes 1–5.

Bailey also suggests that new journals can be categorized in two ways. First, an area of a discipline has grown to a point that it can produce enough papers to support a journal. The publishers' editorial staff must determine the number of papers in the area and whether a publication lag exists that would prevent the timely dissemination of research findings. One of the largest concerns identified by the author is the probability of having sufficient submissions to support the journal publication; additional concerns

include the perceived need and potential support for a new journal in the area. In Volume 1 of *Research on Accounting Ethics*, the articles included not only the papers presented at the first ethics conference, but also, in many cases, the comments of the discussants.

The second category of new journals builds on the synergy involved with having a central publication for all the papers on a specific area rather than have these papers published in numerous other journals. Bailey (p. 197) cites the example of *Arthritis Care and Research* that epitomizes this category of new journals; the justification for this journal was that it ''would focus on research at a different level from that of medical research publications.'' While these concerns screen potential new journals, the critical concern is the ability of the journal to become financially independent, which translates to

> [T]he journal not only must attract subscribers, but also must generate editorial respect, which translates into authors who will submit papers, researchers who will read them and librarians who will endeavor to add them to their collections (p. 197)

This is a real consideration as Bailey points out that it costs approximately $20,000 (i.e., 1989 dollars) in each of the first few years to promote a new journal; these promotion costs can exceed $150,000. Additionally, the growth in the number of new journals makes projecting growth rates much more difficult. The data in Table 1 show that there were 10 business ethics journals being published prior to the first issue of *Research on Accounting Ethics*. Since 1995, 14 additional journals (one of which deals with accounting ethics) were added and four journals have ceased publication – two older and two younger than *Research on Accounting Ethics.*

RESEARCH QUESTIONS

The first research question examines whether the publication of *Research on Professional Responsibility and Ethics in Accounting* and holding the annual Ethics Symposium had any effect on the number of coauthor adjusted business ethics articles authored by accounting faculty.

> **RQ1.** How did the publication of *Research on Professional Responsibility and Ethics in Accounting* and/or having an Ethics Symposium impact the level of published accounting ethics research?

While an increase in the overall level of accounting ethics articles should occur, the publication of a discipline-specific ethics journal could result in a zero-sum game.

Table 1. Ethics Journals by Initial Publication Date.

Title of Journal	First Year
1. *Business & Society*	1960
2. *Business and Society Review*	1972
3. *Business and Professional Ethics Journal*	1981
4. *Journal of Business Ethics*	1982
5. *Ethics and Critical Thinking*	1987
6. *Ethikos*	1987
7. *International Journal of Value-Based Management*	1988
8. *Business Ethics Quarterly*	1991
9. *Business Ethics: A European Review*	1992
10. *Professional Ethics Journal*	1992
11. *Research on Accounting Ethics*	1995
12. *Online Journal of Ethics*	1995
13. *Teaching Business Ethics*	1997
14. *Ethical Theology and Moral Practice*	1998
15. *Journal of Accounting Ethics and Public Policy*	1998
16. *Markets and Morality*	1998
17. *Electronic Journal of Business Ethics and Organizational Studies*	1999
18. *Ethics and Behavior*	1999
19. *Ethics and Information Technology*	1999
20. *Global Virtue Ethics Review*	1999
21. *International Business Ethics Review*	1999
22. *Research on Ethical Issues in Organizations*	1999
23. *Journal of Power and Ethics*	2000
24. *Organizational Ethics: Healthcare, Business and Policy*	2004
25. *Journal of Business Ethics Education*	2004

Notes: Highlighting indicates that the journal is no longer published:

a. The *Online Journal of Ethics* has not published a new issue since the summer of 2000.

b. The *Journal of Power and Ethics* was last published in 2001.

c. *Teaching Business Ethics* and the *International Journal of Value-Based Management* ceased publication at the end of 2003 are now part of the *Journal of Business Ethics*.

d. *Professional Ethics Journal* ceased publication at the end of 2003 and is now part of *Business and Professional Ethics Journal*.

Research on Accounting Ethics was renamed *Research on Professional Responsibility and Ethics in Accounting* in 2004.

Source: Adapted from Bernardi (2005).

RQ2. Did the publication of *Research on Professional Responsibility and Ethics in Accounting* and/or having an Ethics Symposium affect the level of publication of accounting ethics research in other business ethics journals?

METHODOLOGY

In this research, we use the index in Hasselback's (2004) *Accounting Faculty Directory* to identify accounting faculty who graduated from a doctoral program during the 45-year period from 1960 to 2004.[2] We use the criteria Hasselback, Reinstein, and Schwan (2003) employed to stratify our sample into two groups. The first group includes the accounting faculty who received their accounting doctorates from one of the 91 programs listed in Hasselback's (2004) *Accounting Faculty Directory*. The second group of accounting faculty all have doctorates in other than accounting and teach at institutions located in North America.

We used the 23 journals identified by Bernardi (2005, p. 67) and found two additional ethics journals not previously identified (*Ethikos* and *Organizational Ethics: Healthcare, Business and Policy*).[3] These 25 journals have been publishing business ethics research between 45 years (*Business & Society*) and one year (*Journal of Business Ethics Education* and *Organizational Ethics: Healthcare, Business and Policy*).[4] Table 1 lists the 25 business ethics journals and their first year of publication; accounting authors publish in 15 of these journals.

While we restrict our data search to ethics journals, we do not believe this restriction significantly impacts our analysis. For example, we examined articles published in *The Accounting Review* for the period 1980 through 2004 (25 years). We noted that during that time period ethics articles represented less than two percent of the total number of articles published. Similarly, our examination of articles published in the *Journal of Accounting Research*, for the same time period, disclosed that ethics articles comprised less than two percent of the total number of articles published. Possible explanations for these insignificant numbers include: the journals are uninterested in research on the topics about accounting ethics, the journals assume that ethics research has severe methodological flaws, etc. In any event, the lack of inclusion of ethics research in their publications visibly demonstrates that their inclusion or exclusion in the data would not have a significant impact on the results. However, an understanding of the exclusion of ethics research in these and other publications would be a very interesting topic for future research.

Additionally, Cooley and Heck (2005) support our definition and the narrowing of the scope of our research to ethics journals. When debating whether or not to search outside of finance journals in their research, these authors decided going against to journals in real estate, insurance,

economics, and accounting because (bracketed data added by authors):

> Attempting to distinguish finance [ethics] articles from non-finance [non-ethics] articles in those journals would introduce a substantial subjectivity into the analysis (p. 51).

Data Measurement

We count only full articles appearing in these journals and serials – commentaries, replies, notes, and book reviews do not count. We had three choices when it came to data measurement (Bernardi, 2005): full-count articles, coauthor-adjusted articles, and page count. Full-count articles, which give a full-credit publication to each author, inherently overstate the level of publications if any articles are coauthored. For an article with three authors, the number of full-count articles would be three rather than the one actual article. Page count introduces other measurement problems such as page size, font, and character pitch. Consequently, we elected to use the number of coauthored adjusted articles for measurement purposes. The number of authors for an article determined the coauthor-adjusted credit for that article. For example, if there were two (three) coauthors for an article, then each author would receive one-half (one-third) credit for the article. This intuitive reduction also has a theoretical basis; Sauer (1988) notes that the value of a publication with respect to salary is inversely proportional to the number of authors.

Variables

The dependent variable used for both research questions was the number of coauthor-adjusted articles. For the first research question, it was the total number of coauthor-adjusted articles by year from 1985 through 2004. For the second research question, it was the total number of coauthor-adjusted articles for the journals that now comprise either *Business and Professional Ethics Journal* (referred to as B&PE Plus) or the *Journal of Business Ethics* (referred to as JoBE Plus) by year from 1982 through 2004. This combination reflects the fact that *Teaching Business Ethics* and the *International Journal of Value-Based Management* were consolidated with the *Journal of Business Ethics* (i.e., their parent) in 2004. A similar consolidation occurred after 2003 when the *Professional Ethics Journal* again became part of B&PE Plus after 12 years as an independent journal. For example, the *Journal of Business Ethics*, which was initially published in 1982, spun off *Teaching Business Ethics* in 1997, which again became part of the *Journal of Business Ethics* after 2003. Consequently, the combination provides a comparable number of coauthor adjusted articles for the *Journal of Business Ethics*

between the publication dates when *Teaching Business Ethics* was a journal and for the periods between 1982-to-1997 and after 2003.

The independent variables were the publication of *Research on Professional Responsibility and Ethics in Accounting* (RPREA) and our annual Ethics Symposium both of which are indicator variables. For the years between 1982 and 2004 when RPREA was (not) published, RPREA was coded as 1 (0). Similarly, for the years between 1982 and 2004 when the EthSym was (not) held, EthSym was coded as 1 (0).

ANALYSIS

Level of Research Across Time

The first step in the data gathering process was to locate the ethics articles written by accounting faculty and to stratify the data by publication year. Fig. 1 shows the data for the coauthored adjusted ethics articles by accounting faculty members having doctorates either in accounting (squares) or outside of accounting (diamonds); also included is a plot of the combined data (triangles). Again, the use of major in faculty's doctorates is the same factor used by Hasselback et al. (2003) to stratify their sample. For the accounting faculty with doctorates either in accounting or outside of

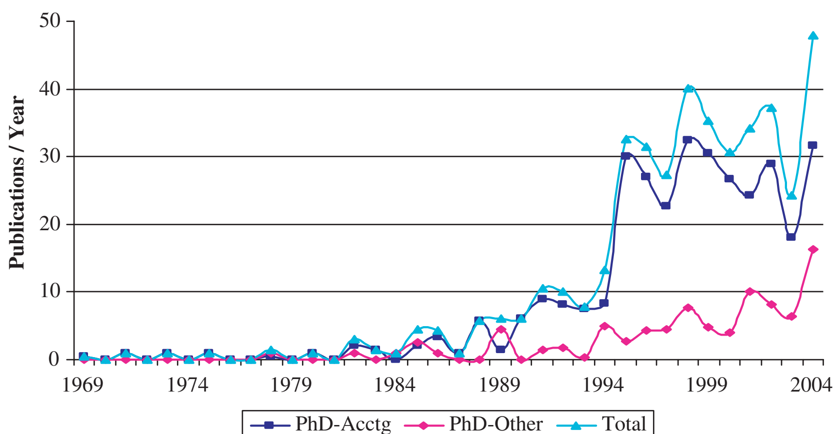

Fig. 1. Level of Accounting Publications in Ethics Journals 1969–2004. *Note:* This figure does not include the publications of the journal editor in the *Journal of Accounting Ethics and Public Policy.*

accounting, there are a series of steps in the data between 1982 and 2004.[5] The data also show that little or no ethics research was published between the start of this study in 1962 and 1980, which supports Lampe's (1996) observation that there was very little emphasis or discussion of ethics prior to the 1980s.

Contemporary Events and Ethics Research

The data in Table 2 provide a historical background surrounding the steps in the level of accounting research published in ethics journals. Table 2 also provides a benchmark by including the number of ethics journals available during each of these periods. The increase in the level of ethics research in the 1982-to-1984 time period is undoubtedly attributable to what some refer to

Table 2. Time Line of Ethics Research.

Timeframe	Coauthor Adjusted Articles/Year	Approximate Rate of Increase in Ethics Research	Number of Journals Available[a]	Contemporary Events
Prior to 1982	$\simeq$0.25	NA	3 [1.6]	The Briloff years
1982–1984	1.75	Seven times	4 [4.0]	
1985–1987	3.25	Double	6 [4.7]	Commission on Sponsoring Organizations (COSO) formed in 1985
1988–1990	6.00	About double	7 [7.0]	Expectation Gap Standards (1988) and First Critical Perspectives on Accounting Conference (1990)
1991–1994	10.40	About double	10 [9.5]	Commission on Sponsoring Organizations of the Treadway Commission (1992) and 1st Symposium on Ethics in Accounting (1996)
1995–2000	33.00	About triple	22 [15.7]	1st issue of *Research on Accounting Ethics* (1995)[a]
2001–2004	36.00	10 percent	20 [21.6]	Enron, WorldCom, and Arthur Anderson

Note: Available journals – number at the end of the period [weighted average during the period].
[a]Renamed *Research on Professional Responsibility and Ethics in Accounting* in 2004.

as the "Briloff" effect. Briloff challenged the accounting profession to critically examine how it was reporting data and making disclosures; he serves as a moral compass for most scholars involved in the ethics research today.

The step that occurred from 1985 to 1987 doubled the prior level of ethics research and coincides with the initial Treadway Commission hearings. The next doubling of the research occurs between 1988 and 1990. These dates coincide with the publication of the "Expectation Gap" auditing standards. The next noticeable increase in the level of accounting ethics research occurs from 1991 to 1994. The first closely follows the first Critical Perspectives on Accounting Conference, which signaled that some of the academy would stand up and be counted by challenging the academy, the large accounting firms, and corporate America.

The most significant change in the pattern occurs in 1995 where there is a dramatic three-to-four-fold increase in the level of ethics research by accounting scholars. This increase coincides with the first issue of *Research on Accounting Ethics* in 1995 and the first Accounting Ethics Symposium in 1995. Our first Symposium and the publication of a journal strictly devoted to publishing research in accounting ethics were significant factors in the increase of accounting ethics research.

Another increase occurred between 2001 and 2002 at the height of the Enron, WorldCom and Arthur Andersen scandals. However, this step represents an increase of only 33 percent when compared to the prior data. It is disturbing to note the minimal impact this event had on published ethics research and the causes of this diminished increase should be investigated. Finally, the decrease in 2003 followed by the dramatic increase in 2004 reflects the fact that *Research on Professional Responsibility and Ethics in Accounting* was not published in 2003; however, it resumed normal publication in 2004.

Modeling the Increase in Ethics Research (RQ1)

The Fig. 2 data display the combined research for the two groups of accounting faculty for the most recent 20 years (i.e., 1985–2004). This is the period in which accounting research published in ethics journals experienced a dramatic sustained increase. The trend line demonstrates the sustained increase that accounting research published in ethics journals has experienced over this 20-year period. Clearly evident in this figure is the significant increase in the level of articles in 1995.

The data in Table 3 show the regression data for the combined sample (Fig. 2). The model used the number of coauthored adjusted articles of accounting research appearing in ethics journals as the dependent variable

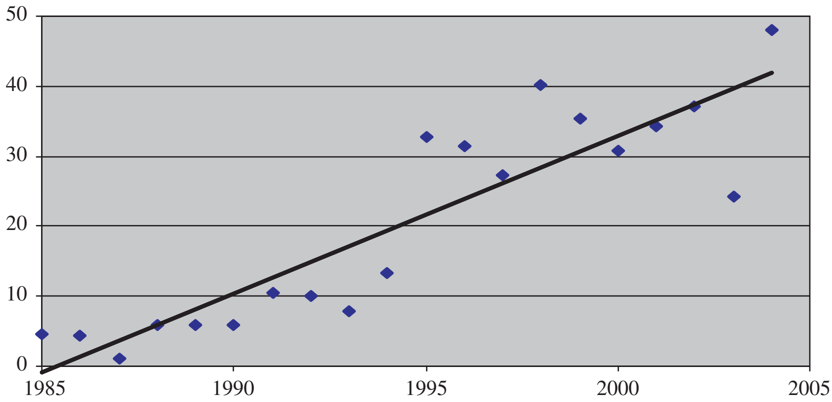

Fig. 2. Graph for Increase in Ethics Research from 1985 to 2004. *Note:* This figure does not include the publications of the journal editor in the *Journal of Accounting Ethics and Public Policy.*

Table 3. Model for Increase in Coauthored Adjusted Ethics Articles between 1985 and 2004 (RQ1).

Model	R^2	Adj. R^2	
Regression	0.950	0.903	
Source	DF	Sum Sq.	*F* Fact
Model	2	3,805.5	78.7
Error	17	411.1	Prob. *F*
Total	19	4,216.5	2.55E-9
Term	Coef.	*T* Stat.	*p*-value
Intercept	6.92	4.45	0.0003
EthSym	17.41	3.38	0.0036
RPREA	10.88	2.10	0.0511

Note: EthSym – an indicator variable: Not held (0), Held (1).
RPREA – an indicator variable: Not published (0), Published (1).

and whether *Research on Professional Responsibility and Ethics in Accounting* (RPREA) was published and whether the Ethics Symposium was held as the independent variables. The data indicate that both ETHSYM ($p = 0.0036$) and RPREA ($p = 0.0511$) significantly increased the level of

coauthor-adjusted articles in accounting ethics research. The model explains 90.3 percent of the variation (adjusted R^2) and indicates an increase of 10.88 coauthored adjusted articles in years that RPREA was published.

Journal-Specific Publication Levels (RQ2)

The data in Table 4 show the level of publication for three ethics journals that published accounting research; we choose these journals because of the changes we noted in their publication records starting in 1995. With the advent of *Research on Professional Responsibility and Ethics in Accounting-RPREA*,

Table 4. Increase in the Number of Coauthored Adjusted Articles in Selected Business Ethics Journals.

Yr	B&PE Plus	RPREA	JoBE Plus
1982	1.0	NP	0.0
1983	0.0	NP	0.5
1984	0.0	NP	0.0
1985	0.0	NP	1.0
1986	1.0	NP	1.3
1987	0.0	NP	1.0
1988	1.0	NP	3.3
1989	0.5	NP	1.0
1990	0.0	NP	6.0
1991	1.0	NP	6.5
1992	1.0	NP	4.7
1993	1.0	NP	5.2
1994	2.0	NP	3.8
1995	6.5	16.8	7.3
1996	4.8	11.7	9.4
1997	0.0	13.7	11.3
1998	1.0	15.1	8.0
1999	1.0	10.2	5.2
2000	0.0	12.7	10.8
2001	1.0	10.7	12.1
2002	0.0	13.0	14.7
2003	1.5	NP	13.2
2004	1.0	8.5	20.2

Note: B&PE Plus: Publications in *Business and Professional Ethics* and the *Professional Ethics Journal* (see Table 1).
RPREA: Publications in *Research on Professional Responsibility and Ethics in Accounting.*
JoBE Plus: Publications in the *Journal of Business Ethics, Teaching Business Ethics* and the *International Journal of Value-Based Management* (see Table 1).
NP: Not published.

there was a reduction in the level of publication in *Business and Professional Ethics* and *Professional Ethics Journal* (referred to as B&PE Plus) both of which had begun to publish a significant level of accounting ethics research. The publication schedule of these journals typically lags other journals by one year (i.e., the 2004 (1996) volume is being (was) published in 2005 (1997)). Consequently, it is not surprising that the effect of RPREA does not appear until 1997. The opposite effect occurs for the JoBE Plus journal group, which increases in 1995. Interestingly, over this 10-year period between 1995 and 2004, the total number of coauthor adjusted articles in the *Research on Professional Responsibility and Ethics in Accounting* and JoBE Plus are essentially identical (112.4 versus 112.2 respectively).

The data in Panel A of Table 5 show the regression model for the level of ethics research published in the JoBE Plus by accounting faculty from 1982 through 2004. During this period from 1995 to 2004, publications by accounting faculty in the JoBE Plus journals significantly increased ($p = 0.0066$) by an average of 10.56 coauthored adjusted articles since the initial Ethics Symposium. The model also shows that the publication of *Research on Professional Responsibility and Ethics in Accounting* was not a significant factor ($p = 0.5414$) on the publication of coauthored adjusted articles in the JoBE Plus journals.

The data in Panel B of Table 5 show the regression model for the level of ethics research published in B&PE Plus by accounting faculty from 1982 through 2004. The model indicates that neither the EthSym ($p = 0.6043$) or *Research on Professional Responsibility and Ethics in Accounting* ($p = 0.9037$) were significant factors on the overall publications in the B&PE Plus journals. This finding may be the result of the short tenure of accounting faculty publishing a large number of articles in these journals (1995 and 1996) and/or that these two years were anomalies.

DISCUSSION

The data in Fig. 2 and Table 3 indicate that the increase in accounting ethics research was not a straight-line progression. Rather the data indicate an increase of 10.88 coauthor adjusted articles between 1994 and 1995 coinciding with the first publication of *Research on Professional Responsibility and Ethics in Accounting.* The data also suggest an increase of 17.41 coauthor adjusted articles relating to the EthSym. Consequently, the growth that the ethics community experienced as a discipline within the accounting academy has been the result of two major events: (1) publishing our own

Table 5. Models for the Effect of RPREA and the EthSym on JoBE and B&PE.

Panel A: Model for the increase in JoBE Plus

Model	R^2	Adj. R^2	
Regression	0.651	0.616	
Source	**DF**	**Sum Sq.**	**F Fact**
Model	2	420.6	18.6
Error	20	225.7	Prob. F
Total	22	646.3	0.0001
Term	**Coef.**	**T Stat.**	**p-value**
Intercept	2.64	2.83	0.0103
EthSym	10.56	3.03	0.0066
RPREA	−2.20	−0.624	0.5414

Panel B: Model for the decrease in B&PE Plus

Model	R^2	Adj. R^2	
Regression	0.111	0.022	
Source	**DF**	**Sum Sq.**	**F Fact**
Model	2	6.0	1.2
Error	20	48.0	Prob. F
Total	22	54.0	0.3805
Term	**Coef.**	**T Stat.**	**p-value**
Intercept	0.65	1.52	0.1436
EthSym	0.85	0.53	0.6043
RPREA	0.20	0.12	0.9037

Note: EthSym – an indicator variable: Not held (0), Held (1).
RPREA – an indicator variable: Not published (0), Published (1).

journal *Research on Professional Responsibility and Ethics in Accounting* and (2) sustaining our annual Ethics Symposium.

The data demonstrate a dramatic increase in the level of ethics research during the 20-year period from 1985 to 2004. However, this period also witnessed a dramatic increase in the number of ethics journals that

published accounting research (Table 1). The question the data suggest is whether the accounting ethics academy can sustain this level of growth, or whether the level of accounting research in ethics journals will level off as it did from 1997 through 2000.

The data in Table 4 suggest that there is additional capacity in *Business and Professional Ethics Journal*. There are also 10 active journals in Table 1, which have not published any accounting ethics research. However, this excess capacity is not enough to sustain our long-range growth at its current pace. In response, one might cite the recent 2004 "Special Editions" of *Issues in Accounting Education* and *Business Ethics Quarterly* that were devoted exclusively to accounting ethics research. If we are to grow as a discipline, we must be proactive in ensuring that ethics research is published in mainstream accounting research journals. The agenda for this is beyond the scope of our research; however, it does present vital research and service opportunities.

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The authors are involved in several research projects and alternate lead author responsibilities; both authors contribute equally to all of their published works.

NOTES

1. The first ethics journal *Business & Society* inaugural issue was in 1960; consequently, our study spans the 45-year period between 1960 and 2004.
2. There were no articles published by accounting faculty during the period from 1960 through 1968 in *Business & Society* (i.e., the only business ethics journal prior to 1969).
3. Even though we identified two additional journals, there were no articles in these journals authored by accounting faculty.
4. The implicit assumption here is that all publications in these journals are ethics articles.
5. The dataset is incomplete as we are missing two issues of the 2004 volume of the *Business and Professional Ethics Journal*, which typically lags one full year.

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ETHICAL EARNINGS MANAGEMENT TRAINING: THE INFLUENCE OF DECISION CONTEXT EFFECTS

John C. Anderson, Sudip Bhattacharjee and Kimberly K. Moreno

ABSTRACT

Given the recent publicity surrounding corporate earnings management behavior, a relevant question is whether training would be beneficial as a way to increase sensitivity to ethical issues. However, in order to develop effective training activities, a better understanding of the fundamental psychological principles that impact training is needed. Research in psychology and decision making indicates that contextual information that a person brings to a decision (e.g., ethics training cases) may influence a person's judgment. This study investigates whether exposure to earnings management cases as a training tool will impact managers' intentions to engage in subsequent earnings management behavior. Using full-time and part-time students with an average of 3.4 years business experience, we find that those exposed to a prior positive ethical training context were more likely to indicate an intention to undertake subsequent earnings management behavior than those exposed to a prior negative ethical training context. Moreover, since individuals may differentially process

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contextual information, additional results show that participants' need for cognition (a personal characteristic) interacts with context effects. Implications for designing training are discussed.

Ethical decision-making research supports the importance of ethics training (e.g., Abdolmohammadi, 2005). However, in order to develop efficient and effective training activities in any context, we need a better understanding of fundamental psychological principles that impact training (Quinones & Ehrenstein, 1997). Since one goal of ethics training is to increase awareness of ethical issues (Thorne LeClair & Ferrell, 2000; Jones, Massey, & Thorne, 2003; Beauchamp & Bowie, 1997), instructional materials often contain examples of both positive and negative ethical behavior. This training material may provide a context upon which future ethical decisions are made. Research in psychology suggests that contextual information that a person brings to a decision may influence a person's judgment (e.g., Higgins, 1996; Manis, Nelson, & Shedler, 1988; Stapel & Koomen, 1998). In effect, the context in which a target stimulus is evaluated provides a framework for the evaluation (Stapel & Winkielman, 1998). Therefore, it is important to understand the influence of one psychological factor, contextual information, on ethics training.[1]

Context effects occur when the context in which individuals encounter information provides an interpretative frame for subsequent evaluations and judgments (Stapel & Winkielman, 1998). Context effects are particularly prevalent when the target stimulus is ambiguous (e.g., Higgins, 1989, 1996) such as in earnings management judgments that typically involve no clear right or wrong answer. Earnings management issues have been receiving a great deal of attention from academics and practitioners in light of recent accounting and corporate scandals. Regulators are particularly concerned, since these activities can be misleading and detrimental to financial statement users. Since many types of earnings management activities are not clearly acceptable or unacceptable, an important question is whether these activities are the right thing to do (Merchant & Rockness, 1994). In fact, earnings management may be one of the most important ethical issues facing the accounting profession (Merchant & Rockness, 1994). Management's ethics are called into question when they engage in earnings management activities (Bruns & Merchant, 1990). To reduce the likelihood of these activities, a relevant issue is whether exposure to earnings management cases as a training tool would be beneficial. Therefore, this study investigates whether the exposure to prior positive or negative contextual training

information differentially impacts the subsequent likelihood of earnings management behavior.[2] In addition, since prior ethics research suggests that *need for cognition* (NFC) can influence ethical judgments (Boyle, Dahlstrom, & Kellaris, 1998; Singer, Mitchell, & Turner, 1998), we examine whether this individual characteristic mediates or exacerbates the influence of context effects during ethical earnings management training.

To investigate these issues, 127 participants with an average of 3.4 years business experience first read a training case describing the ethical financial reporting style of a company (i.e., non-aggressive or aggressive) that was intended to create either a positive or negative context. Thereafter, all participants read an ambiguous earning management case on a different company in which they were a senior manager. They then rated the ethical quality of the earnings management behavior and how likely they would be able to undertake a request to manage earnings in the current year. The results indicate that individuals who were exposed to the positive-oriented ethical training context were more likely to undertake the request to manage earnings than participants who were exposed to the negative-oriented ethical training context for the same earnings management situation. Additional results show that high need for cognition (HNFC) individuals were more influenced by context effects than low need for cognition (LNFC) individuals.

These results demonstrate the influence of prior contextual information when participants with professional business experience undertake a realistic and ambiguous earnings management judgment. Specifically, exposure to positive-oriented ethical training information made participants less conservative in their subsequent ethical earnings management judgments in an ambiguous situation than exposure to negative-oriented ethical information. These results add to our understanding of factors that can impact ethics training in accounting (Jones et al., 2003). These results also extend prior ethics research by examining the likelihood of individual's ethical *behavior* in an earnings management situation since prior ethics research has primarily focused on ethical perceptions of earnings management activities (e.g., Elias, 2002; Fischer & Rosenzweig, 1995; Merchant & Rockness, 1994). Similarly, these results extend prior decision-making research by demonstrating contexts effects on the likelihood of individuals' *behavioral ratings* as opposed to *ratings* of events or people, the primary focus of prior research (e.g., Geiselman, Haight, & Kimata, 1984; Strane & Watts, 1977). This issue is particularly relevant for the earnings management context since regulators and investors are ultimately concerned with management's behavior. These findings have implications for designing training tools that could be used to moderate earnings management behavior.

LITERATURE REVIEW

Ethics Training for Earnings Management

In light of recent accounting and corporate scandals, earnings management continues to receive a great deal of attention from academics and practitioners and remains a significant concern for investors, regulators, auditors and management (e.g., Shafer, 2002). Earnings management has been defined as intentional non-neutral financial reporting by management to obtain some private gain (Schipper, 1989). In general, earnings-based bonus plans and restrictive debt covenants can create economic incentives for managers to manage earnings. Managers can manage earnings by timing or structuring transactions or by changing their interpretation of financial accounting standards (Healy & Wahlen, 1999).

Since many earnings management tactics are within the guidelines of generally accepted accounting principles (i.e., GAAP) and involve significant latitude in judgment, a key feature of the earnings management definition is managerial intent. Therefore, engaging in earnings management raises concern about management's ethics (Bruns & Merchant, 1990). In fact, Merchant and Rockness (1994) argue that earnings management may be one of the most important ethical issues confronting the accounting profession. Given the serious ethical issues surrounding earnings management judgments, some studies have begun to examine factors that may influence ethical judgments in this domain.

In specific, several studies have examined earnings management ethics across various user groups (e.g., managers, shareholders, internal auditors, students) (Kaplan, 2001a, 2001b; Merchant & Rockness, 1994; Elias, 2002; Fischer & Rosenzweig, 1995). In general, these studies have found that ethical perceptions of various earnings management activities vary by respondent type. For example, Merchant and Rockness (1994) found that managers judged earnings management behavior least ethically, while internal auditors judged the activities most favorably. Research also suggests that practitioners judge earnings management behavior more harshly than students (Fischer & Rosenzweig, 1995). Other research has shown a relationship between personal moral philosophies, social responsibility and earnings management ethics. For example, Elias (2002) found that individuals who believed in social responsibility rated earnings management activities more unethical than other individuals. In general, these studies suggest that individual factors can influence ethical perceptions of earnings management activities.

Given the gravity of earnings management issues, it is surprising to note that little research has considered the influence of training on ethical decision making in this domain. Ethics training is designed to increase employee knowledge, skills and decision making in the ethics area (Thorne LeClair & Ferrell, 2000). In specific, ethics instruction should raise an employee's awareness of the ethical issues in various situations (Beauchamp & Bowie, 1997; Velasquez, 1998). Therefore, an important question is whether increased sensitivity to ethical earnings management issues will influence ethical decision making.

While a variety of instructional methods are used in ethics training, the most popular forms include lectures and videotapes (Shandler, 1996). This passive form of training indicates that much of the information conveyed is probably standardized information in the form of examples of both positive and negative ethical behavior (e.g., whistleblowing and fraud). Research suggests the need for a better understanding of the factors that may impact ethics training (including fundamental psychological principles) in order to develop efficient and effective training activities (Jones et al., 2003; Quinones & Ehrenstein, 1997). Thus, when evaluating the outcomes of various training methods, psychological aspects, including cognitive, affective and skill-based factors, must be considered (Kraiger, Ford, & Salas, 1993). For example, research in other domains suggests that contextual information (e.g., ethical instructional material) that a person brings to the earnings management decision may influence the likelihood of a person's earnings management behavior (e.g., Higgins, 1989, 1996). Therefore, an important issue is how this contextual ethical training information may influence the likelihood of future ethical behavior in the earnings management domain. This study extends prior earnings management ethics literature by examining the influence of exposure to ethical training information on individuals' likelihood to engage in earnings management.

Context Effects

Most individuals would agree that our evaluations and judgments are experienced contextually and determined by their relationships to other evaluations made in the past. In effect, the context in which a target stimulus is embedded provides an interpretive frame for evaluation (Stapel & Winkielman, 1998). As a result, the same target stimulus can be evaluated differently depending on the context in which it is judged.

Context effects have been documented in social cognition and social-judgment research (e.g., Higgins, 1996; Manis et al., 1988), marketing

research (e.g., Rashmi & Monroe, 2002) and strategic decision making (Highhouse, Paese, & Leatherberry, 1996; Stapel & Koomen, 1998). For example, Srull and Wyer (1979) primed participants with words like ''hostility'' or ''kindness'' and found that individuals who were primed with hostility rated an ambiguous target person more hostile than participants who were primed with kindness. Similarly, in studies of physical attractiveness, the same face has been judged to be more attractive when presented alongside attractive faces than when presented with unattractive faces (Geiselman et al., 1984; Strane & Watts, 1977). Research in marketing also indicates that consumers' responses are influenced by the description associated with an accessible contextual cue (e.g., Herr, 1989; Meyers-Levy & Sternthal, 1993).

Several explanations have been proposed to explain context effects. Previous judgments may form mental anchors, and subsequent judgments may represent inadequate adjustments from those anchors (e.g., Gregory, Lichtenstein, & MacGregor, 1993; Highhouse et al., 1996). Context effects are also consistent with research on priming and category accessibility (Smith & Branscombe, 1987; Wyer & Srull, 1981) in which the prior context creates a prime or category which is then used as the standard of comparison in subsequent judgments. Adaptation level theory (Helson, 1964) uses the concept of norms and proposes that a stimulus is evaluated by comparing it to the norms that it evokes; thus, each event brings its own frame of reference. While several theories can be used to explain context effects, it is important to note that all of the theories consistently note that judgments are not made in a vacuum, but rather are interpreted by a contextual frame of reference.

It should be noted that context effects can result in both assimilation effects (i.e., target is rated similar to the context) or contrast effects (i.e., target is rated different to the context). Research indicates that numerous factors can influence whether assimilation or contrast effects will occur (Foti & Hauenstein, 1993). Most relevant to the current study, assimilation effects occur when factors tend to emphasize the similarity between the target and context or cause people to consider the target and context as one unit, whereas factors that emphasize the differences between the target and context cause people to compare the two (Cooke, Sujan, & Weitz, 2002). Stapel, Koomen, and Velthuijsen (1998) operationalized this notion in a marketing domain and demonstrated that assimilation effects will occur when the contextual information consists of attributes (e.g., inexpensive) and contrast effects will occur when the contextual information consists of specific examples (e.g., Suave Shampoo). Since our contextual manipulation consisted of ethical earnings management attributes (e.g., questionable financial

reporting practices), we believe that an assimilation effect is relevant to the current study.

Furthermore, Foti and Hauenstein (1993) found that increased processing demands increased the possibility of finding assimilation effects. The complex earnings management case used in the current study also supports the prediction of assimilation effects. As noted earlier, our primary focus is on the influence of context effects on the likelihood of behavior rather than just their ethical ratings. Therefore, we believe that individuals who are exposed to prior positive ethical training information will be more likely to *rate* an ambiguous ethical earnings management decision more positively and thus be more likely to *undertake earnings management behavior* than individuals who are exposed to a prior negative ethical training context.

Context Effects in Ethical Earnings Management Behavior

We believe that studying context effects during ethical earnings management training is an interesting area for several reasons. Prior research indicates that context effects are particularly prevalent when the target stimulus is ambiguous (e.g., Higgins, 1989, 1996; Stapel & Koomen, 1998; Wyer & Srull, 1989). In effect, there is more to interpret when the target is ambiguous rather than unambiguous. Many ethical earnings management decisions involve gray judgments where there is no clear right or wrong answer. As a result, individuals' earnings management decisions are likely to be influenced by the context in which they are made. That is, individuals who are exposed to negative accounting reporting practices during training may view earnings management tactics more negatively and be less likely to manage earnings than individuals who are exposed to positive accounting reporting practices during training. Based on this idea of ambiguous judgments, it is likely that the earnings management domain is one ethical area that context effects will have a particularly strong effect.

The earnings management context is also important to investigate since this domain addresses the behavioral implications of context effects. That is, investors and regulators are concerned with earnings management behavior. Interestingly, prior research on earnings management ethics has primarily focused on individuals' ethical perceptions rather than their actual intention to engage in earnings management activities (e.g., Elias, 2002; Fischer & Rosenzweig, 1995; Merchant & Rockness, 1994; Kaplan, 2001a, 2001b). Similarly, prior research on context effects generally has not focused on how individuals' behavior is affected (Boyle et al., 1998). Rather, the context research has primarily examined the influence of context effects on

individuals' ratings of people or events. While research indicates that an ethical judgment is a factor in the formation of a behavior (e.g., Chiu, 2003), prior ethics research in accounting also suggests that the formation of an ethical behavioral intention may be more complex than simply building from an evaluation of an action's morality (Cohen, Pant, & Sharp, 2001; Shafer, 2002).

For example, Cohen et al. (2001) found that in certain contexts accounting professional and students were willing to take a questionable business action in spite of their overall evaluation of the action as relatively unethical. Shafer (2002) contends that economic factors may have a more pronounced effect on ethical behavior than on ethical judgments. He contends that the specific separation of ethical judgments from behavior in the Rest (1986) and Jones (1991) models is based on the assumption that practical considerations may lead to behaviors that are inconsistent with an individual's evaluation of what is ethically right or wrong. Empirical results from Shafer (2002) confirm that, despite moral reservations, participants felt there was a significant probability that corporate executives would succumb to organizational pressures to fraudulently misstate financial information, particularly when the amounts were quantitatively immaterial. The potential discrepancy between an individual's ethical evaluation and ultimate ethical behavior is particularly important in the earnings management context since investors and regulators are ultimately concerned with ethical earnings management behavior. Therefore, the current study extends both the ethics and decision-making literatures by examining the influence of context effects on both individuals' ethical judgments and likely behavior in the earnings management domain. The following hypotheses are formally tested:

H1a. Individuals who receive prior ethical training information on negative reporting practices will rate the ethical quality of a subsequent earnings management scenario more negatively than individuals who receive prior ethical training information on positive reporting practices.

H1b. Individuals who receive prior ethical training information on negative reporting practices will rate their likelihood of managing earnings lower than individuals who receive prior ethical training information on positive reporting practices.

Need for Cognition

While the prior discussion suggests that contextual information will influence ethical decision making, prior ethics research also suggests that NFC,

an individual characteristic, can influence ethical judgments (Singer et al., 1998; Boyle et al., 1998). NFC refers to an individual's tendency to engage in and enjoy effortful cognitive endeavors (Cacioppo & Petty, 1982). While most researches have focused on the situational factors that determine when individuals think effortfully or more heuristically (Cacioppo, Petty, Feinstein, & Blair, 1996), individual differences represent an additional source of variation. This may be particularly important when dealing with context effects from ethics training since individuals may differentially process contextual information. That is, individuals HNFC tend to seek, acquire and think about information to make sense of stimuli, relationships and events; individuals LNFC are characterized as more likely to rely on others or social comparison processes to provide this structure (Cacioppo & Petty, 1982, 1984; Cacioppo, Petty, Kao, & Rodriguez, 1986).

Numerous research indicates that HNFC individuals recall more of the information that they are exposed to, are more responsive to argument quality, and less responsive to peripheral cues than LNFC individuals (e.g., Boehm, 1994; Priester & Petty, 1995). On the basis of this evidence, it might appear that the information processing activity of HNFC individuals would be more objective and impartial than that of LNFC individuals. However, research on priming and primacy effects indicates that HNFC individuals' judgments can be more influenced by priming information than LNFC individuals (Kassin, Reddy, & Tulloch, 1990; Meyers-Levy & Tybout, 1997). Petty and Jarvis (1996) argue that HNFC individuals are more susceptible to priming than LNFC individuals because HNFC individuals have greater memory for and think more about the contextual information than LNFC individuals.

In the ethics domain, Singer et al. (1998) found that HNFC individuals demonstrated a greater utilization of issue-relevant information. In effect, they found that HNFC individuals deliberated more on the characteristics relevant to the moral issue. Similarly, Boyle et al. (1998) found that HNFC individuals were more likely to process and use priming information as a point of reference against which to judge a target situation. Based on the prior discussion, we believe that during ethical earnings management training HNFC individuals will be more susceptible to context effects than LNFC individuals. The following hypothesis is formally tested.

H2. High need for cognition individuals will be more influenced by context effects than low need for cognition individuals during ethical earnings management training.

METHODOLOGY

Participants

One hundred and twenty-seven participants took part in the study by completing an earnings management case. The participants were graduating seniors ($n = 65$), and graduate students enrolled in full-time ($n = 32$) and part-time ($n = 30$) courses at a public university. The graduating seniors were non-traditional students who had worked before returning to school full-time, were working full-time while attending school part-time or had participated in co-operative programs or internships. Therefore, these graduating seniors had more work experience than traditional students. The graduate students were enrolled in graduate business programs in which work experience was a prerequisite for admission.

The average business work experience across all participants was 3.4 years, indicating that these individuals had the relevant experience to make informed business judgments. It is also important to note that the graduating seniors were accounting majors and our graduate participants were either MBAs or Masters of Accounting students. Therefore, they had the accounting and business knowledge to make an informed decision given the complexity of the experimental case. The participants were divided into two groups (i.e., either the negative or the positive ethical context group).

Experimental Procedures

In order to examine the impact of exposure to ethical contextual training information on earnings management decisions, individuals first read information describing the ethical financial reporting style (i.e., non-aggressive or aggressive) of a company that was intended to create either a positive or negative context. Participants were told that this case was part of an ethical business-training workshop. Thereafter, all participants read and evaluated an ambiguous earnings management case on a different company in which they were a senior manager. Participants were asked to rate the ethical quality of the proposed earnings management behavior and to indicate their likelihood of undertaking the earnings management behavior described in the case.

Ethical Training Information

Participants in both the negative and the positive ethical context conditions first read a training case on a company (Universal Inc.) and its industry.

The company manufactured electronic components primarily used in the automotive industry. Thereafter, individuals read information that was intended to create either a strongly positive or a negative ethical context. In the negative context condition, participants were told that the company had a very aggressive financial reporting style that was attributable to the CFO (named David East). The CFO had set a tone at the top that focused on achieving performance targets through almost any means. The participants were also told that the CFO had undertaken some questionable financial reporting practices to meet bonus targets. Specifically, the CFO had demanded that the company's small distributors purchase additional merchandise at a significant cost, which they would not have to pay for until it was sold to their customers. However, this transaction was recorded as sales by Universal Inc. in violation of the GAAP. In general, the negative context indicated that the company followed questionable financial reporting practices and was not fair in dealing with its distributors.

The positive context group was provided with similar information to the negative context group except in the opposite direction. That is, individuals in the positive context group were told that the company's CFO had set a tone at the top of accurate and high quality financial reporting and delivering quality goods at a fair price. In addition, the CFO was very sensitive to the needs of his distributors and believed that his company should be a responsible member of the community. Participants were told of a specific instance where the CFO was concerned that some of his divisional managers were recording revenue prematurely. Given that the CFO wanted to be open and truthful about the company's financial reporting, he made it very clear that sales were only to be recorded when all aspects of the revenue recognition process had been virtually completed. In other words, participants who read the positive information were provided with a context of fair play and open and truthful financial reporting.

After reading the context information, all participants responded to a manipulation check question that had them rate the ethical quality of the CFO's financial reporting behavior to verify that the positive or the negative context effects had been achieved. The manipulation check is particularly relevant since participants may have come into the study with a heightened awareness of earnings management issues owing to the recent publicity given to various corporate scandals. Once the manipulation is achieved, the relevant comparison for this study would be between the negative and positive groups since it is difficult to design a context-free group to serve as a baseline. To ensure that participants processed the contextual information in the context manipulation, we also had them list the three factors that

most significantly influenced their opinion about the ethical quality of the CFO's financial-reporting behavior.

Earnings Management Case

After receiving the context manipulation, all participants read information on a *different* company (Regency Manufacturers) that manufactures and sells a variety of industrial products in which they were a Senior Manager. The case indicated an ambiguous earnings management situation where the CFO (named Reed) of the company wanted to postpone certain discretionary expenses. Participants were told that the CFO wanted to raise capital early in the next year through a public offering to fund capital expansion and a new R&D project. Further, the CFO believed that the stock issuance would be successful only if the financial performance in the current year was strong. To allow the company to meet its profit targets, the CFO requested that the participants shift some discretionary expenses from the current year to the next year. While the expenses were discretionary, postponing these expenses in the current year would mean that these expenses would eventually be incurred in the following year.

To create a situation where the appropriateness of postponing the expenditures was ambiguous, participants received information that both supported and refuted the CFO's proposed actions. For example, the information indicated that, while the postponement may raise earnings management concerns, it did not violate current accounting standards and the company's external auditors had no objection to postponing the expenses. In addition, deferring the expenses would allow the company to raise capital and invest in new projects, which could increase the company's future profits. However, if the expected investments in R&D and capital investment projects did not payoff, next year's financial statements would show a sharp drop in profit due the poor performance on the projects and the eventual incurrence of the deferred expenses. Since postponement of the expenses would not be disclosed, shareholders would not know that the positive financial results in the current year were due in part to a potential earnings management tactic. We chose an ambiguous earning management situation to follow the ethical training information because we wanted to create a salient shift from the earlier context. In this way, both experimental groups read the same earnings management case, and the judgments of participants in both context groups could be directly compared.

After reading the earnings management case, participants were asked to rate how likely they would be to undertake the CFO's (Reed's) request to

postpone expenses in the current year without disclosure in the financial statements on an 11-point scale (-5 = not very likely; 5 = very likely). This was the main dependent variable of the study used to determine if the nature of the prior ethical training material (negative or positive) differentially impacted the actual decisions made in a subsequent ambiguous earnings management situation. For consistency with the manipulation check question and prior ethics and context effects research (e.g., Chiu, 2003; Cruz, Shafer, & Strawser, 2000; Barnett & Vaicys, 2000), participants were also asked to rate the ethical quality of postponing the discretionary expenditures. After responding to the dependent variable, all participants responded to demographic questions by listing their years of business experience, GPA and age. Finally, participants responded to the NFC scale developed by Cacioppo and Petty (1982). The scale is a widely used 18-item instrument that measures people's tendency (on a scale ranging from -5 to 5) to engage in and enjoy effortful cognitive endeavors (see Cacioppo et al., 1996 for a review). The scale items can be represented in terms of a single factor called NFC. The Cronbach's Alpha of this measure was 0.93, thus demonstrating its reliability. There were no differences in the NFC scores between participants in the positive ethical context group (mean = 22.15; SD = 19.06) and the negative ethical context group (mean = 17.24; SD = 19.65) [$t = 1.19$; $p > 0.23$].

RESULTS

We discuss the results of the manipulation check and the demographic questions prior to presenting the main results. Based on the ethical training case, the manipulation check question asked individuals to rate the ethical quality of the CFO's (David East's) behavior on an 11-point scale (-5 = very Unethical to 5 = very ethical). Participants who were provided with the positive context information rated the quality of the CFO's behavior as significantly more ethical (mean = 3.54) than individuals who received the negative context information (mean = -3.6) [$t = 18.52$; $p < 0.001$]. Thus, participants who were provided with negative ethical contextual information developed a significantly more negative context than participants who were provided with positive ethical information, indicating that the context effect manipulation was successful.[3]

Table 1 presents demographic data for each experimental group including gender, number of graduate students and graduating seniors, business experience, age, and GPA. The results indicate no significant difference in the

Table 1. Demographic Variables.

Variable	Positive Context $n = 61$	Negative Context $n = 66$	p Value
Class	Graduate students = 50.8% Graduating seniors = 49.2%	Graduate students = 43.9% Graduating seniors = 56.1%	0.475[a]
Gender	Female = 39.3% Male = 60.6%	Female = 50% Male = 50%	0.258[a]
Mean business experience (in years)	3.1	3.7	0.515[b]
Mean age	24.5	23.9	0.510[b]
Mean GPA	3.19	3.13	0.525[b]

[a] = χ^2 test p value.
[b] = T-test p value.

proportion of graduate students and graduating seniors between the groups ($p > 0.47$). No significant differences were observed in the proportion of male and female participants between the groups ($p > 0.26$). In addition, the years of business experience between the positive-context group (mean = 3.1) and the negative-context group (mean = 3.7) did not differ significantly ($p > 0.51$). No significant differences were observed in the average age between the positive-context group (24.5) and the negative-context group (23.9) ($p > 0.51$), as well as in the mean GPA between the positive (mean = 3.19) and the negative (mean = 3.13) context groups ($p > 0.52$). This demonstrates the equivalence between the two-experimental groups.[4]

Context Effects in Ethical Earnings Management Training

Prior to responding to the main dependent variable, participants were asked to rate the ethical quality of the CFO's (Reed's) request in the ambiguous earnings management case (Regency Manufacturers) on an 11-point scale (−5 = very unethical to 5 = very ethical). These results are presented in Table 2. The mean ethical quality rating of the CFO's request for individuals who were earlier exposed to the negative context was –1.58, while the mean rating of individuals who were earlier exposed to the positive context was −1.03 for the same earnings management case ($t = 1.29$; $p < 0.098$). While the differences between the groups are marginally significant, the results demonstrate an assimilation effect with the positive-context group rating the behavior as more positive and the negative-context group rating the behavior as more negative. These results provide marginal support for H1a. It is important to note that participants in both groups evaluated the questionable earnings management behavior as unethical. In fact, the mean

Table 2. Context Effects in Ethical Earnings Management Training.

Variable	Positive Context $n = 61$	Negative Context $n = 66$	t Statistic	p Value[a]
Ethical quality rating[b]	−1.03	−1.58	1.29	0.098
(−5 = very unethical to 5 = very ethical)	(2.44)	(2.29)		
Likelihood of postponing expenses[c]	−0.11	−1.33	2.38	0.009
(−5 = not very likely to 5 = very likely)	(2.85)	(2.89)		

Note: Means (Standard Deviations) and *T*-test.
[a] *T*-tests are one-tailed.
[b] Participants were asked to rate the ethical quality of the CFO's request to postpone expenses, knowing that this information will not be disclosed in the financial statements.
[c] Participants rated how likely they were to undertake the request to postpone expenses, knowing that this information will not be disclosed in the financial statements.

ratings of both the negative-context group (mean = −1.58) and the positive-context group (mean = −1.03) were significantly lower than zero, the neutral mid-point of the scale ($p < 0.05$). Therefore, while context effects had a marginal influence on evaluations, participants overall rated the behavior as unethical.

Table 2 also presents the results of the main dependent variable that examines the ethical earnings management behavioral ratings. Participants were asked to indicate how likely they would be to undertake the CFO's (Reed's) request to postpone the expenditure without disclosure (−5 = not very likely to 5 = very likely). As indicated in Table 2, the prior context significantly influenced the likely earnings management behavior of the participants. Individuals who were exposed to the positive context were more likely to undertake the request to postpone the expenses (mean = −0.11) than participants who were exposed to the negative context (mean = −1.33) for the same earnings management situation ($t = 2.38$; $p < 0.009$). Thus, H1b is supported since exposure to a negative ethical training context made participants more conservative in their actual decisions in an ambiguous earnings management situation than exposure to a positive prior ethical context. This is significant, given that many earnings management decisions involve gray judgments where there is no clear right or wrong answer, and no judgment is context-free. In our experimental setting, our results indicate that the earnings management decisions of individuals with work experience are likely to be influenced by the exposure to prior contextual training information.

It is also important to consider that, consistent with prior research (Shafer, 2002), participants' likely behavior was influenced by context effects

in spite of their overall evaluation of the action as relatively unethical. These findings suggest that despite moral reservations, participants' likely earnings management behavior was influenced by context effects. These results demonstrate the importance of examining both evaluations and the likelihood of behavior in ethical accounting decision-making contexts.

To provide further insight into the association between participants' ratings of the ethical quality of the earnings management case and their subsequent likely behavior, we regressed participants' ethical quality ratings on their behavior ratings. The overall regression ($F = 80.81$, $p < 0.001$) is significant, indicating that participants' ethical quality ratings influenced their behavior ratings. In fact, ethical quality ratings accounted for a substantial amount of variation in likely behavior ($\beta = 0.782$, $t = 8.99$, $p > 0.001$; $R = 0.628$). Therefore, while context had a marginally significant effect on ethical quality ratings, these regression results suggest that there is a significant relationship between ethical quality ratings and likelihood of behavior. However, consistent with prior research, other factors (e.g., context effects) besides the judged morality of the action may lead to behaviors that are inconsistent with a person's conception of what is morally right and wrong.

Additional Analysis: Test for Social-Desirability Response Bias

Given the nature of the questions asked in this study, we needed to verify that participants' responses were not affected by a social-desirability response bias (Randall & Fernandes, 1991; Cohen, Pant, & Sharp, 1996; Geiger & O'Connell, 2000). When responding to an experimental question, participants may overstate their intention to act in an ethical manner in order to appear to be more altruistic and society-oriented than is actually the case. Social desirability response bias can exist even in cases where respondents are anonymous (Randall & Fernandes, 1991). This is primarily because this bias results from the desire to over-report activities that are deemed to be socially or culturally desirable and the desire to under-report activities that are deemed to be socially or culturally undesirable (Zerbe & Paulhus, 1987). The heightened awareness toward earnings management issues due to recent audit failures can lead individuals to take a culturally desirable position that earning management is not acceptable. Thus, in this study, participants may have overstated their intention to act in an ethical manner when responding to the question on their potential earnings management behavior.

Accounting ethics researchers have tested for this bias by comparing responses to the question "Would you do it?" with responses to the question "Would your peers do it?" with respect to undertaking a questionable action

(e.g., Cohen, Pant, & Sharp, 1998; Beams, Brown, & Killough, 2003; Jones et al., 2003). The bias should not be present in a question about one's peers because it does not directly reflect on the respondent. Thus, consistent with prior research, we test for the social-desirability response bias by comparing the response to the question "How likely are you undertake the request to postpone expenses in the current year?" (the main dependent variable) with the response to the question "How likely are your peers to undertake the request to postpone expenses in the current year?" (Cohen et al., 2001; Beams et al., 2003).

To perform this test, we asked a subset of 41 participants from this study (19 from positive-context group; 22 from negative-context group) to respond to an additional question indicating "How likely do you believe that *your peers* are to undertake Reed's request to postpone 1999 expenses, knowing that this information will not be disclosed in the financial statements?"(-5 = not very likely; 5 = highly likely). The results indicate that for the positive-context group there were no significant differences between participants' response to the question would your peers undertake the request to postpone the expenses (mean = 0.70; SD = 2.97) and the overall response to the question, "would you undertake the request to postpone the expenses?" (mean = -0.11; SD = 2.85) ($t = 1.07$; $p > 0.29$). Similarly, for subjects assigned to the negative context group, no significant differences were observed between the question, "would your peers undertake the request to postpone the expenses?" (mean = -0.94; SD = 2.64) and the overall response to the question "would you undertake the request to postpone the expenses?" (mean = -1.33; SD = 2.89) ($t = -0.51$; $p > 0.61$). This indicates that social desirability response bias was not a factor in this study. More importantly, the main finding of the study that exposure to prior positive or negative contextual training information differentially influences the subsequent likelihood of earnings management behavior also holds for the likelihood of *peers'* behavior. That is, exposure to a prior positive context during training led to significantly higher perceptions of peers' engaging in earning management behavior (mean = 0.70; SD = 2.97) than exposure to a prior negative context during training (mean = -0.94; SD = 2.64) [$t = 1.80$; $p < 04$]. This confirms the robustness of our main results.

Interaction of Context Effects and Need for Cognition

Table 3 examines whether higher NFC individuals will be more susceptible to context effects when making ethical earnings management judgments than lower NFC individuals.[5] To examine this issue, we first assigned

participants to a low or a HNFC group depending on their NFC score. Participants with NFC scores below the median NFC score of 22 were assigned to the low NFC group, while participants with above the median NFC scores were assigned to the high NFC group. Thereafter we estimated the following regression separately for the low and the high NFC groups:

$$\text{POSTPONE}_i = \alpha_0 + \alpha_1 \text{D}_{\text{CONTEXT}\ i} + \varepsilon_t \quad (1)$$

POSTPONE_i is the likelihood of postponing expenses rating for individual i (same variable as Table 2), while $\text{D}_{\text{CONTEXT}\ i}$ is a dummy variable equal to 1 if individual i was assigned to the negative ethical context group, and 0 if individual i was assigned to the positive ethical context group. α_1 represents the association between the likelihood of postponing expenses rating and the prior training context.

Table 3 reports separate regression results of equation (1) for the LNFC and HNFC groups. For the LNFC group, the estimated coefficient for α_1 was not significant indicating no significant relationship between postponement of expenses and the prior training context. For the HNFC group the

Table 3. Regression Coefficients from the Test of Likelihood of Postponing Expenses and the Need for Cognition Score[a].

	Estimated regression coefficients [b] $\text{POSTPONE}_i = \alpha_0 + \alpha_1 \text{D}_{\text{CONTEXT}\ i} + \varepsilon_t$			
	Low NFC		High NFC	
	Intercept	$\text{D}_{\text{CONTEXT}}$	Intercept	$\text{D}_{\text{CONTEXT}}$
Coefficient estimate	−0.25	−0.542	−0.583	−1.89
t-value	0.39	−0.63	−1.01	−2.24*
	$R^2 = 0.09$ Adjusted $R^2 = 0.02$		$R^2 = 0.11$ Adjusted $R^2 = 0.09$	

[a]This table reports regression estimates of the likelihood of postponing expenses on the prior training context separately for the low and the high need for cognition (NFC) groups. Participants with NFC scores that were below the median were assigned to the low need for cognition (LNFC) group, while participants with above the median NFC scores were assigned to the high need for cognition (HNFC) group.

[b]Description of regression variables:

POSTPONE_i = The likelihood of postponing expenses rating for individual i.

$\text{D}_{\text{CONTEXT}\ i}$ = A dummy variable equal to 1 if individual i was assigned to the negative ethical context group and 0 if individual i was assigned to the positive ethical context group.

$* = p < 0.05$.

estimated coefficient for α_1 was significant ($t = -2.24; p < 0.03$) indicating a significant relationship between postponement of expenses and the prior training context. The coefficient α_1 indicates that for the HNFC group, participants who were exposed to a prior negative-ethical context indicated a greater likelihood of postponing expenses (i.e., a more aggressive behavior) than participants who were exposed to a prior positive-ethical context. Thus, H2 is supported since HNFC individuals were more influenced by context effects than LNFC individuals during ethical earnings management training.[6] Overall, our results indicate that exposure to ethical contextual training information may influence the likelihood of earnings management behavior of individuals with work experience. In addition, NFC interacts with context effects.

CONCLUSION

In this paper, we examined whether the exposure to prior positive or negative contextual training information differentially influences the likelihood of earnings management behavior of participants with business experience. Within the constraints of an experimental setting, our results suggest that ethical training information can have a significant influence on individuals' likelihood to manage earnings in an ambiguous situation. Individuals who were first exposed to a negative ethical context (i.e., aggressive financial reporting attributes) were more conservative in their likelihood to manage earnings than individuals who were first exposed to a positive ethical context (i.e., non-aggressive financial reporting attributes). These findings are significant since many earnings management decisions involve equivocal situations. Results also suggest that individual characteristics, specifically NFC, can have an interactive influence on context effects in earnings management decisions. HNFC individuals were more susceptible to context effects than low NFC individuals.

The results of this study extend both the ethical earnings management and context effect literatures. Prior ethical earnings management research has primarily focused on individuals' ethical perceptions of various earnings management activities (e.g., Elias, 2002; Fischer & Rosenzweig, 1995; Merchant & Rockness, 1994). This study illustrates that ethical training information can influence individuals' likelihood to manage earnings. In effect, the training context a person brings to an earnings management judgment could have a significant influence on the likelihood of behavior. These findings are particularly relevant since earnings management continues to

receive an extensive amount of attention from investors, regulators and auditors. This heightened awareness to earnings management tactics suggests that ethics training as a means of reducing these activities may receive more attention in the future. Since passive exposure to ethical training scenarios is a likely training tool, the influence on context effects is an important issue to consider when designing ethics training cases.

This study also increases our understanding of context effects. Prior research has primarily focused on the influence of context effects on individuals' *ratings* of events or people (Geiselman et al., 1984; Strane & Watts, 1977). However, our results suggest that context effects also can influence the likely *behavior*. In effect, individuals' likely behavior assimilated toward the prior context. This study demonstrates the pervasive and significant influence context effects can have on decision making. In addition, it is important to consider that context effects seemed to have a stronger influence on the likelihood of participants' behavior than their ethical-quality ratings. Future research needs to consider situations in which ethical-quality ratings of earnings management may be more or less influenced than earnings management behavior.

As with any experimental research, the current study has limitations, which in some cases offer opportunities for future research. A limitation is that, while in practice there may be a time delay between receiving training and facing an actual ethical dilemma, we could not have had the same type of time delay in our study due to the constraints of the experimental setting. Future research could consider examining the influence of ethical training on a longitudinal basis. For example, participants could be provided with the training cases at the start of a semester and given the neutral earnings management scenario later in the semester. Using the current study as a baseline, the results of such a study would indicate the impact of context effects of ethics over time.

The results of this study have implications for both research and practice. In practice, consideration of the type of ethical training material (i.e., positive or negative) should be given since this can influence the resulting behavior. For example, based on the results of the current study, it appears that negative ethical training cases may result in more conservative earnings management behavior, while positive ethical training cases may result in less conservative earnings management behavior. In addition, given calls for a better understanding of the factors that may impact ethics training in accounting (Jones et al., 2003), the findings from this research indicate that both psychological factors and individual characteristics (e.g., need for cognition) should be considered in the development of training.

NOTES

1. While ethics training can involve many methods, passive learning through lectures and presentations is a common instructional method (Shandler, 1996). As a result, sensitivity as a training tool is popular and is a likely situation where contexts effects could occur.

2. In this study, we examine managers' behavioral intentions to engage in earnings management activities (i.e., likelihood of behavior) rather than actual behavior. Due to the impossibility of carrying out investigations into unethical conduct in the workplace, many research studies use intention as their operational variable (Chiu, 2003). The theory of planned behavior suggests that behavioral intention is a good predictor of actual behavior (Ajzen, 1991). In fact, a meta-analysis of 87 research studies utilizing a behavioral intention measure indicates that these measures perform well in the actual prediction of behavior (Sheppard, Hartwick, & Warshaw, 1988).

3. Only four participants in the positive-context group had a negative score in the manipulation check, while only three participants in the negative-context group had a positive score in the manipulation check. The results of the study would remain unchanged if these participants were excluded from the analysis.

4. We ran several analyses to ensure that demographic factors did not impact the results of our study. In specific, we ran 2 separate 2X2 ANOVAs with context (negative/positive) and participant type (undergraduate/graduate) as factors on the dependent variables of interest (ethical-quality rating and behavior rating). Neither the main effect for the participant type variable nor the interaction of participant type and context were significant in either ANOVA indicating that there were no differences in the responses between either participant groups. In addition, we reanalyzed our results by separately including years of business experience and age as covariates in our analysis. The covariate variables were not significant ($p > 0.1$). Taken together, this indicates that participant type, years of business experience, and age did not impact the results of the study.

5. Due to constraints on participants' time, individuals in the part-time graduate class ($n = 30$) did not complete the NFC scale. Therefore, the NFC analysis needed to be performed separately excluding this group (in Table 3). As a check, we excluded this group of participants and reanalyzed the results of the main dependent variable (Table 2). The results were consistent with those reported in Table 2.

6. Similar analyses were conducted with participants' ethical quality ratings as the dependent variable. However, the results of the regression were not significant. Given the insignificant results, and more importantly, the focus of the current study on the likelihood of earnings management behavior, the results of this regression are not reported.

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AUDITOR REPUTATION AND INDIVIDUALS' INVESTMENT DECISIONS

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ABSTRACT

We conduct an experiment to investigate whether concerns about an auditor's reputation affect individuals' investment decisions. Importantly, insurance is absent in our setting, which allows us to focus on perceived audit quality. We examine participants' decisions to invest in companies audited by Andersen, which suffered irreparable damage to its reputation. Participants allocate cash across a set of investment opportunities and are paid based on the actual performance of the companies they invest in. We provide information sheets for each investment opportunity, which indicate that the firm received a "clean opinion" audit report. For one group of participants the auditor's identity is concealed, while in the second group the auditor's identity is revealed. A comparison across groups allows us to determine whether individuals' decisions are affected by their knowledge of the auditor's identity. We find that participants invest less in a company once they know Andersen is the auditor, apparently because Andersen is perceived to provide a lower quality audit than other major accounting firms.

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This paper reports the results of an experiment designed to investigate the effect of perceived audit quality on portfolio allocation decisions. For users of financial statements, audit quality is not observable. Users must make inferences about audit quality, most often relying on auditor characteristics. If a reputable auditor certifies a company's financial statements, the perceived quality of the audit and, in turn, the credibility of financial data is strengthened. We examine whether individuals' assessments of a company's auditor affect their decisions to invest in the company.

Auditor reputation can be impaired as a result of various events, including bad press, lawsuits, and government sanctions. The extent to which concerns about audit quality affect investors' behavior, however, is unclear. A fundamental issue is whether impairments to auditor reputation undermine the credibility of financial data and erode investors' confidence in a company's performance. The issue is pertinent in light of recent, highly publicized accounting scandals, which have caused the investing public to question audit quality in general: that is, whether the audit function adds sufficient credibility to financial statements.

Recent accounting scandals caused such a stir that the Sarbanes–Oxley Act of 2002 was enacted to restore investors' faith in the credibility of audited financial statements. A substantial portion of the Act is aimed at improving audit quality and, in turn, enhancing auditor reputation in general.[1] To gain insight into the effect of auditor reputation impairments, we investigate individuals' decisions to invest in companies audited by Andersen.

Obviously Andersen suffered irreparable damage to its reputation as a result of the Enron scandal; however, descriptive data do not suggest that Andersen's audit quality was inferior to that of other large accounting firms. In a study of Securities and Exchange Commission (SEC) accounting and auditing enforcement releases (AAERs) in the U.S., Bannister and West (2001) report that the frequency of times that Andersen is named is comparable to that of other large auditors.[2] Likewise, a study of peer review reports, for auditors of SEC registrants in the U.S. in the early 1990s, indicates that Andersen did not receive a single modified report: i.e., peer review reports did not find any instances of reduced audit quality on Andersen's part (General Accounting Office, 1996).

Archival data suggest that those investing in clients of Andersen reacted negatively to the Enron scandal. Chaney and Philipich (2002) provide evidence that Andersen's clients, on average, experienced negative abnormal returns around various news releases.[3] But it is difficult to determine whether the negative returns are attributable to impairments of the auditor's reputation (i.e., concerns over lowered audit quality) or concerns over the

auditor's ability to provide insurance (refer to Baber, Kumar, & Verghese, 1995). Our study focuses on reputation impairment: whether being audited by Andersen as opposed to another large auditor affects users' beliefs about the reliability of financial data.

We study the effect of auditor reputation impairments apart from the auditor's ability to serve as an insurer. Individuals' willingness to invest in a company, or the price that an individual is willing to pay for stock, can be affected by (1) the credibility of the financial data attested to by the auditor and (2) the auditor's ability to cover losses (i.e., the auditor as an insurer that financial data are not materially misstated).[4] We are interested in the former because reputation impairments occur much more frequently than auditors' inability to settle claims (i.e., auditor bankruptcy).[5] We directly examine whether being associated with Andersen affects users' willingness to invest in firms when individuals do not have the option of suing the auditor to recoup losses.

The remainder of this paper is organized as follows. First, we outline why concerns about audit quality influence investor behavior. Next, we describe the experimental method and then present the results. Lastly, we summarize our findings, discuss implications for the profession, and provide suggestions for future research.

PRIOR RESEARCH AND HYPOTHESIS DEVELOPMENT

Historically, users of financial statements have viewed large auditors favorably. Companies typically switch to a major firm prior to public stock offerings (Carpenter & Strawser, 1971). Beatty (1989) documents higher stock prices in initial public offerings for companies audited by large accounting firms as compared to those audited by others (see also Balvers, McDonald, & Miller, 1988; Michaely & Shaw, 1995). Teoh and Wong (1993) provide evidence that earnings are perceived to be more credible for companies audited by major accounting firms as opposed to those associated with other auditors. Finally, researchers report that large auditors earn audit fee premiums, which suggests that companies are willing to pay more for brand name auditors (e.g., Simon & Francis, 1988; Craswell, Francis, & Taylor, 1995; Bandyopadhyay & Kao, 2001).

Though large auditors are perceived as providing high quality services, they are not infallible. Sometimes their work is publicly criticized or sanctioned and occasionally audit failures occur. Limited research has examined the economic consequences of events that impair the auditor's

reputation. Firth (1990) provides evidence that companies associated with auditors who are criticized in government reports experience a small, but statistically significant wealth loss when the reports are publicly disclosed. Others provide conflicting evidence (e.g., Wilson & Grimlund, 1990; Lennox, 1999). The current study focuses on companies associated with Andersen, which suffered greatly from the Enron debacle. We investigate whether Andersen's reputation or image was damaged to the extent that individuals' might question audit quality and show a reluctance to invest in companies it audits, absent the ability to sue the auditor.[6]

To provide background, we summarize a chronology of events, occurring in the U.S., which impacts the investing public's assessments of Andersen. The year 2001 was very tumultuous. Andersen settled large lawsuits in connection with its audits of Sunbeam and Waste Management and was fined $7 million by the SEC. Enron also began to unravel in 2001. On October 17 Enron reported a third-quarter loss. On November 9 Enron disclosed that earnings had been overstated by approximately $600 million since 1997. On December 2 Enron filed for bankruptcy protection. Further, on December 12 Andersen's CEO, Joe Beradino, admitted an error in judgment in his testimony before Congress. As 2001 came to an end, the *New York Times* reported that the year had easily been the worst in Andersen's history (Norris, 2001).

Unfortunately, matters only worsened in 2002. On January 10, Andersen admitted to destroying incriminatory evidence. On March 15, a criminal indictment was filed against the auditor. In May, a large civil lawsuit was settled in connection with the audits of the Baptist Foundation of Arizona (at the time the second largest settlement in history). Finally, on June 15 Andersen was convicted on one count of obstructing justice (though this conviction was later overturned in 2005 by the U.S. Supreme Court). Needless to say, the auditor's reputation was severely damaged.

Investors likely have negative affective reactions upon learning that Andersen is a firm's auditor. Adolphs and Damasio (2001, p. 45) describe *affect* as a representation that incorporates the value of a stimulus or action to an individual. For our purposes, affect refers to an evaluative image that is evoked in response to Andersen being associated with the audit of a company.

The series of highly publicized events surrounding Andersen creates a very unflattering image of the auditor and likely evokes a negative affective reaction from even the most casual (novice) investor. For the investor, mental representations of Andersen are likely tagged to varying degrees with affect and stored in memory (e.g., Damasio, 1994; Finucane, Alhakami, Slovic, & Johnson, 2000). Because of Andersen's well-documented problems, the affect tagging is likely associated with unfavorable outcomes

(e.g., Gelernter, 1994). The financial data of companies audited by Andersen, for instance, may be viewed skeptically (i.e., as having less credibility).

Importantly, research suggests that affective and emotional aspects play a fundamental role in assessing information and guiding decision-making (e.g., Zajonc, 1980; Schwarz & Clore, 1988; Damasio, 1994; Elster, 1998; Isen, 2000). For the investor, contexts that involve Andersen are likely to activate information stored previously, bringing a negative-affective reaction to mind. The investor then may make inferences about audit quality and the reliability of financial data. Though audit quality is not observable, individuals likely perceive that greater uncertainty surrounds the financial reports of companies audited by Andersen. Our experimental sessions were conducted subsequent to Andersen's indictment for obstructing justice and, as such, participants may have been leery of firms audited by Andersen. We suggest that individuals shun companies that are audited by Andersen – because of uncertainty surrounding the trustworthiness of financial data. Our hypothesis (in alternate form) is expressed as follows:

> $\mathbf{H_a}$. Individuals invest a lower proportion of total funds in a company when they believe that the company's auditor is not reputable, absent insurance concerns (i.e., the possibility of recovering losses from the auditor does not exist).

RESEARCH METHOD

Overview

We conduct a one-shot "investment" experiment. An experimental approach allows control for factors that potentially create challenges for archival researchers. Importantly, we are able to carefully regulate the information available on these companies – specifically the auditor's identity. In our experiment, participants make investment decisions that have real economic consequences. Participants are endowed with cash, which they allocate among a set of investment opportunities. They are paid at the end of the experiment based on the actual performance of the companies they invest in. By focusing on economic decisions (i.e., those that directly impact participants' wealth), we are able to determine whether concerns about audit quality have a meaningful effect on individuals' behavior.[7]

We vary the information provided on each investment opportunity. Our experimental design includes two groups. In the first group, the auditor's

identity is concealed (referred to as the Base group). This group provides a benchmark and serves as a basis of comparison to assess investor behavior. In the second group, the auditor's identity is revealed (referred to as the AudID group). A comparison of the two groups allows us to determine whether individuals' investment decisions are affected by their knowledge of the auditor's identity: that is, Andersen versus another large auditor. All other information on the potential investment opportunities is *held constant* across the two groups.

Participants

We recruited 47 students from a medium-sized university in the U.S. to participate in the experiment: 23 in the Base group and 24 in the AudID group. The students include undergraduates and graduates (masters), with the vast majority (91 percent) in at least their third year of university studies. Seventy-nine percent of the participants are business students. Participants have a mean age of 25.2 years and have completed or are currently enrolled in an average of 2.9 accounting courses and 2.5 finance courses.[8] Eighteen participants (or 38 percent) have previously traded securities or taken part in the management of an investment portfolio. Participants earn on average $33.06 for taking part in the study, which required 60–75 minutes to complete.[9]

Procedures

We conducted four experimental sessions, two for each group. The sessions were conducted on June 12 and 13, 2002. Each experimental session proceeds as follows. The instructions are distributed and read aloud by the experimenter. According to the instructions, participants are endowed with $1 million in cash and asked to allocate the funds among the set of six available stocks. Participants may choose not to invest in a particular security, but they may not short sell. So that they would take the exercise seriously, participants were told that at the end of the session they would be paid based on the actual performance of the companies in which they invested.

Participants are given an information sheet on each investment opportunity, including a brief narrative of the firm's operations, the firm's standard industrial classification (SIC), selected financial information, and historical and current stock prices. In each case (across the six firms and the two groups), the information sheet indicates that the firm received a "clean opinion" audit report.[10] Specific information on auditor identity differs between the two groups – otherwise the information is identical.

Participants are instructed that the information sheets are developed using data from the annual reports of actual companies for fiscal years ended in 2001. To conceal the firms' identities, five-character alphanumeric codes are used to identify the investment opportunities. Participants are informed that two of the six firms announced an earnings restatement three months after fiscal year end, though they are not told which two companies so that earnings restatement effects are not confounded with auditor reputation effects. They are told that the two firms revised their earnings number downward and, in turn, experienced a negative stock price reaction. For these two firms, stock price three months after fiscal year end was below that at year-end. Participants are also told that for the other four firms, stock price three months after fiscal year end was above that at year end.

Participants are allotted 35 minutes to review the information sheets and make their portfolio-allocation decisions.[11] They invest at current stock prices, so their initial portfolio is worth $1 million. After making their investment decisions, participants complete an experimental questionnaire. They assess several factors on 11-point scales, including beliefs about the future prospects of specific industries, auditor quality, and factors affecting the quality of audited financial statements. We also ask participants to identify factors they considered relevant in making their investment decisions.

Subsequently, the final prices are announced: the closing price actually observed three months after fiscal year end. Participants liquidate their portfolios at these prices and are paid 0.000030 times the ending portfolio value. After computing their ending portfolio values, participants complete a post-experiment questionnaire designed to collect demographic information. Lastly, participants are paid and dismissed.

Selection of Firms Included in Investment Opportunities

Several steps were taken in selecting the six firms included in the set of investment opportunities. First we identified two firms with earnings restatements. We searched newspaper archives in the U.S. and focused on restatements that (1) occurred three months after fiscal year end (many restatements coincided with the announcement of first quarter earnings), (2) were for earnings reported in 2001, (3) were for firms that were not easily recognizable, and (4) were for firms audited by a Big Five auditor.[12] We restricted our focus to firms that received a "clean opinion" audit report and had positive cash flows from operations and positive earnings per share for the most recent fiscal year (to facilitate matching with firms that did not have restatements). For firms with restatements, we restricted our focus to

Table 1. Firms Used in the Study.

Firm[a]	SIC Code	Auditor Identity
American Power Conversion[b]	3600	KPMG
Genlyte Group	3600	Andersen
Excel Technologies	3600	Ernst & Young
CryoLife[b]	3800	Andersen
Zoll Medical	3800	Ernst & Young
Varian Medical Systems	3800	PricewaterhouseCoopers

[a]A five-character alphanumeric code was used to denote firms in the experimental materials.
[b]These firms had earnings restatements.

those that experienced a downturn in stock price: the stock price following the announcement of the earnings restatement was less than that at fiscal year end. This last requirement makes it explicit that, in making investment decisions, participants should avoid firms that subsequently restate earnings.

For each restatement firm, we chose two comparable firms, selected based on two-digit SIC codes. We excluded firms that would be easily recognizable.[13] The firms must have received a "clean opinion" audit report and had positive cash flows from operations and positive earnings per share for its fiscal year ending in 2001. The comparable firms also had to experience an upturn in stock price: the stock price three months after fiscal year end was greater than that at fiscal year end. In selecting firms, we did not include any auditor more than twice.

The six firms selected for the study and disguised for the participants are identified in Table 1, including relevant information for each firm. For the Base group, each firm's auditor is characterized generically as a Big Five auditor. For the AudID group, each firm's auditor is revealed. As shown, two firms are audited by Andersen, two by Ernst & Young, and one each by KPMG and PricewaterhouseCoopers. Within each two-digit SIC code, each firm contracts with a different auditor.

RESULTS

Main Findings

The mean proportion of funds invested per company for the two experimental groups is shown in Table 2. Our research hypothesis implies that individuals invest a lower proportion of funds in companies if they have knowledge that Andersen is the auditor. The data indicate that for the two

Table 2. Investment in Firms.

Firm[a]	Auditor Identity	Group[b]	
		Base Group	AudID Group
American Power Conversion	KPMG	0.095 (0.105)	0.096 (0.090)
Genlyte Group	Andersen	0.248 (0.232)	0.203 (0.163)
Excel Technologies	EY	0.168 (0.226)	0.132 (0.112)
CryoLife	Andersen	0.189 (0.178)	0.146 (0.122)
Zoll Medical	EY	0.093 (0.110)	0.200 (0.144)
Varian Medical Systems	PwC	0.208 (0.238)	0.224 (0.226)

[a]A five-character alphanumeric code was used to denote firms in the experimental materials.
[b]Cell entries indicate the mean proportion (standard deviation) of investment in each firm.

companies audited by Andersen, the proportion of funds invested is less when the auditor's identity is revealed. A parametric t-test indicates a marginally significant difference between the Base and AudID groups ($t = 1.35$, $p = 0.093$, one-tailed test): the mean investment in the two companies audited by Andersen is 0.436 for the Base group and 0.349 for the AudID group, resulting in a difference of \$87,000 ($0.087 \times \$1$ million) for the two groups. This result provides modest support for our hypothesis.

We also examine the rank of the funds invested in the companies audited by Andersen. For each participant, we rank their investment allocations from one to six, with one assigned to the company that is allocated the most money, two to the company that is allocated the next most money, and so forth. Hence, a higher sum of ranks indicates a lower amount of investment. Our hypothesis suggests that the sum of the ranks for the two Andersen clients is greater for the AudID group than for the Base group. A t-test indicates a statistically significant difference ($t = 2.53$, $p = 0.008$, one-tailed test): the mean rank of the Base group is 4.78 and the mean of the AudID group is 5.71. This result provides further support for our hypothesis.

Supplementary Analysis

To determine whether participants had a negative image of Andersen, we investigate their responses to the experimental questionnaire. Participants

Table 3. Participants' Perceptions of Auditor Quality.

Auditor	Mean[a] (Standard Deviation)
Andersen	4.64 (2.79)
Ernst & Young	7.60 (1.65)
KPMG	6.87 (1.66)
PricewaterhouseCoopers	8.04 (1.63)

[a]Participants responded on an 11-point scale, with endpoints of 1 = low quality and 11 = high quality.

were asked to rate the four auditors on 11-point scales: the endpoints of the scales were 1 = low quality and 11 = high quality. The mean responses, shown in Table 3, indicate that Andersen is perceived to provide lower quality than the other three auditors. We perform a repeated measures analysis of variance, with the dependent measure being the rating assigned to each auditor. Planned contrasts indicate that Andersen is rated lower than each of the other auditors at $p < 0.001$. We repeat the analysis using the rank of each auditor's rating as the dependent measure and the results are similar. Moreover, we find that 36 of 47 participants (or 77 percent) assigned the lowest relative rating (i.e., relative to the other auditors) to Andersen. Hence, participants had a negative image of Andersen as an auditor relative to the other major accounting firms.[14] The results reported in the main analysis are consistent with those reported in Table 3. Participants in our experiment invested less in firms audited by Anderson, and Anderson's audit quality received the lowest rating by a majority of subjects.

CONCLUSION

We conduct an experiment to investigate the effect of perceived audit quality on participants' investment decisions. The findings should be considered in light of possible limitations such as small sample sizes (24 in one group and 23 in the other) and a limited investment opportunity set of six firms. Our results indicate that participants invest less in companies audited by Andersen, which suffered irreparable damage to its reputation. Because our experiment did not allow participants to sue the auditor to recoup investment losses, our findings are consistent with participants ascribing a lower

quality or credibility to financial data audited by Andersen. Responses to a post-experiment questionnaire provide further support: participants' responses indicate that they perceive that Andersen provides a lower quality audit than the other major accounting firms. One implication of our finding is that the negative abnormal returns experienced by Andersen clients, as documented in archival studies (e.g., Chaney & Philipich, 2002) is attributable, at least partially, to concerns over audit quality and the associated credibility of reported financial data. Interestingly, Moreland (1995) reports that SEC sanctions in the U.S. against the auditor lower client companies' earnings response coefficients: news that reflects poorly on the auditor's reputation results in market participants assigning less credibility to financial data. Our results are consistent with this finding and suggest that users' investment decisions are affected if the auditor's reputation is impaired. Therefore, investors should consider the reputation of audit firms when making investment decisions, knowing that the investment demand for the particular company may be affected by its audit firm's reputation.

This research on the effects of auditor reputation can be extended in a number of ways. In addition to the Big CPA firms examined in this study, future research can study reputation effects of other national firms, as well as regional and local firms. This study included audit opinions on the fairness of financial statements. Now that the Sarbanes–Oxley Act of 2002 requires auditors to provide opinions on companies' internal controls, these opinions can be included as well in future research. Aside from investing decisions, future studies can also address whether lending decisions are affected by auditor reputation.

NOTES

1. Among other things, the Act (1) establishes the Public Companies Accounting Oversight Board, which oversees and investigates the audits and auditors of public companies, (2) mandates annual quality reviews of auditors that audit more than 100 public companies, (3) prohibits the auditor from performing most non-audit services, (4) requires rotation of the lead audit partner every five years, and (5) prescribes that the auditor attest to management's assessment of the effectiveness of internal control.

2. In a study of AAERs involving financial fraud, Beasley, Carcello, and Hermanson (1999) report that from 1987–1997 only 10 cases in the U.S. involved a large auditor (i.e, the auditor is named in the AAER). The study, however, does not report the results partitioned by accounting firm and subsequent communication with the authors indicates that data on the auditor's identity was not collected.

3. For example, abnormal returns of roughly two percent are attributed to Andersen's admission of destroying documents related to the Enron audit.

4. Individuals may be reluctant to invest in a company if they are leery of financial data or concerned that they will be unable to sue the auditor if financial data are inaccurate.

5. From time to time, auditors suffer reputation impairments, for example, due to public censure, media coverage, or litigation. Auditor bankruptcy, however, is an extremely rare occurrence.

6. We focus on the behavior of individual investors because this subset of market participants is significant and potentially impacts security prices (e.g., DeLong, Shleifer, Summers, & Waldman, 1989, 1990, 1991; Shleifer & Summers, 1990; Shapira & Venezia, 2001). According to the New York Stock Exchange (2002), approximately *34 million individuals* invest directly in the stock market. Brennan (1995) argues for increased attention on the individual investor to enrich our understanding of financial markets and institutions. Bossaerts (2001) underscores the importance of properly modeling individuals' beliefs to appropriately characterize market outcomes (see also Daniel, Hirshleifer, & Subrahmanyam, 1998; Hirshleifer, 2001).

7. Research in economics indicates that hypothetical and real decisions do not always coincide (e.g., Bohm, 1994; Cummings, Harrison, & Rutstrom, 1995; Holt & Laury, 2002). Research in psychology also suggests that the association between attitudes and behavior is often tenuous (Wicker, 1969; Ajzen & Fishbein, 1980).

8. Nine participants had previously completed an auditing course. Inferences are unaffected if these participants are excluded from the analyses (reported in the next section of the paper).

9. We compare the demographic characteristics of participants in the two groups and find no statistically significant differences.

10. A ‘‘clean opinion’’ audit report is defined as being issued when the auditor determines that financial statements present fairly the firm's financial position and results of operations and cash flows in accordance with prescribed standards.

11. Pre-tests indicate that 35 minutes is sufficient to allow participants to review the information sheets and make their investment decisions.

12. This last requirement is not particularly restrictive. As reported in CFO.com (Radigan, 2002), 97 percent of publicly traded companies and mutual finds registered with the SEC are audited by what is now the Big Four.

13. Our final selection of firms resulted in six relatively small firms, with none having total assets in excess of $1.4 billion.

14. Further analysis fails to produce significant differences in participants' perceptions (i.e., responses to other items on the experimental questionnaire) between the two groups.

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FACULTY ETHICS CODE EXPECTATIONS: AN EMPIRICAL SURVEY OF U.S. ACCOUNTING DOCTORAL PROGRAMS

Alan K. Styles and Thomas E. McKee

ABSTRACT

Extensive press coverage of wide ranging ethical problems in business during recent years has created an "ethical crisis" for the accounting profession and accounting education. Historical ethical hallmarks such as independence, integrity, and objectivity have been widely questioned. Current AACSB accounting accreditation standards require accounting academic units to establish expectations for ethical behavior by administrators, faculty, and students.

This article addresses the question of how accounting faculty ethical expectations have been and could be established. We identify areas where accounting faculty have ethical issues, review-related literature, and discuss alternative ways accounting faculty can establish clear faculty ethical expectations, including providing a comprehensive, internationally developed, accounting faculty ethical code for benchmarking. Two linked nationwide surveys of the 70 active U.S. accounting doctoral programs were conducted to determine how formal accounting faculty ethical expectations are currently being established.

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The two national surveys found that no accounting doctoral programs had a separate accounting faculty ethical code. Separate comprehensive business school faculty ethical codes which apply to all business faculty were found for only two of the 70 accounting doctoral programs. All schools had at least one university level ethical code. The lack of separate accounting program and business school ethical codes suggests that formal accounting faculty ethical expectations are currently primarily established at the university level. The sufficiency of university level ethical codes is an open question that warrants a further dialogue within accounting academia.

Newspaper headlines about the business world during the past few years have trumpeted ethical problem areas such as the following:

• Corporate accounting	Enron (CNN.com, 2004)
• Corporate auditing	Arthur Andersen (*ibid.*)
• Insider trading	Samuel Waksal, ImClone Systems (MSNBC, 2004)
• Lying to investigators	Martha Stewart (*ibid.*)
• Mutual fund trading-	Janus Mutual Funds (New York State Attorney General, 2004)
• Defective aircraft parts	Boeing Company (Arizona U.S. Attorney, 2004)
• Stock analysts' forecasts	Jack Grubman of Salomon Smith Barney (Securities Law.Com, 2004)
• Corporate looting	Dennis Kozlowski of Tyco (Court TV.Com, 2004)
• Excessive pay	Richard Grasso of NYSE (Batterson, 2004)

The frequency, economic effects, and extensive publicity related to ethical problems, such as those previously listed, have created what could be considered an "ethical crisis" in business and accounting. Many in academia believe that although business practice has problems, the problems in academia are few or that academics are somehow "above it all" (Borkowski & Gaffney, 1995, p. 3). However, critics have said that "… most business schools have failed to respond proactively" and have a "… history of sidestepping ethics" (Swanson, 2005, p. 247). We believe the ethical crisis extends to business schools and especially to accounting education.

The accounting academic community has responded to the "ethical crisis" in ways such as:

- increasing ethics coverage in courses,
- adding new courses on ethics,
- holding seminars on ethics,
- conducting research in ethics,
- formulating or enforcing "ethical codes of conduct" for students,
- publishing the journal *Issues In Accounting Education* "Special Issue on Professionalism and Ethics in Accounting Education" during February, 2004 (Gaa & Thorne, 2004, pp. 1–2), and
- formulating international standards for the ethics education of professional accountants (IFAC, 2004).

Most of this effort focuses on ethics related to students. Little of this effort is focused on the accounting faculty themselves. Yet it has been asked, "… if academicians can effectively teach ethics to others if their profession has not adequately examined its own ethical behavior?" (Crain & Carruth, 1992, p. 28). Others argue "… that academicians should exhibit a higher degree of professionalism and adhere to a more strict code of ethics than other professions" (Bruhn, Zajac, Al-Kazemi, & Prescott, 2002, p. 465) and "[I]t is reasonable to hold academics to a high moral standard, as they are in a prime position to influence young minds through their modeling and control of information" (Bruhn et al., 2002, p. 471).

The failure to turn the spotlight on ourselves as academics after major business failures is a continuing rather than just a recent problem. More than a decade ago Crain and Carruth (1992) stated, "[A] great deal of attention has been focused on unethical practices in business and government. The role of ethics in academia, particularly academic research, has been largely ignored" (p. 27). More recently Meyer and McMahon (2004) stated, "[I]n light of the recent scandals involving accountants, academic accountants should step to the forefront to address our own issues to assure that we will not experience our own Enron" (p. 441). Loeb and Merino (2000) considered the implications that

> [I]n occupations and professions that have not formally established a code of ethics a degree of ambiguity exists as to what might be viewed as ethical norms and behavior. We have noticed over the years that discussions relating to ethical norms and ethical behavior for faculty members frequently cause discomfort among some colleagues … [T]here is no definitive formal ethical code for faculty members in higher education (the academy) in the United States (p. 293).

We believe there are a large number of areas where accounting faculty members potentially could have ethical problems, including

- Research misconduct plagiarism, e.g. falsifying data/results or research.
- Sexual misconduct, e.g. harassing students for sexual favors.
- Racial misconduct, e.g. discriminating against minorities or acting on the basis of racial stereotypes.
- Dealing with ethical issues surrounding student misconduct cases, e.g. not following formal university policies.
- Unethical teaching behaviors, e.g. canceling classes for unapproved personal reasons, inattention to teaching, giving inappropriate preference to student athletes, or intentionally making a class too demanding to create a high drop rate which results in a more desirable small class to teach.
- Fund-raising behaviors, e.g. giving preference to donor's child in academic program.

The ethical problems are not restricted to accounting academics. All academics face problems of the previous types. However, the important question is how accounting academics choose to face up to their ethical responsibilities.

The current AACSB accreditation eligibility standards state: "The accounting academic unit must establish expectations for ethical behavior by administrators, faculty, and students." An AACSB interpretation of this standard then states, "Academic units are encouraged to develop 'codes of conduct' to indicate the importance of proper behavior for administrators, faculty, and students in their professional and personal actions" (AACSB, 2005, p. 5).

There are primarily three ways by which accounting academic units could establish ethical expectations:

1. Establishment of a separate accounting academic unit ethical code. This code could either be completely self-contained or it could reference other codes and only include additional expectations for issues not appropriately addressed in other codes.
2. Reliance on a separate business school ethical code.
3. Reliance on university, state, and/or professional ethical codes, which may apply to accounting faculty.

Any of these three approaches might prove to be satisfactory if the ethical expectations are comprehensive enough and clearly communicated.

Many believe that accounting Ph.D. programs should be at the forefront of ethical developments and training since they are educating and training

future accounting educators (Meyer & McMahon, 2004, p. 414; Loeb, 1994, p. 192; Crain & Carruth, 1992, p. 28). An open question appears to be how formal accounting faculty ethical expectations are currently being established for these programs? Our research investigates this issue via two linked nationwide surveys of the 70 active U.S. accounting doctoral programs. This paper reports on the results of these nationwide surveys.

LITERATURE REVIEW

The literature on ethics in education may be divided into two main categories. One section of the literature basically examines the past, present, and future role of ethics in education of students at U.S. colleges and universities. This includes an examination of what has gone wrong in the business community that led to ethics scandals, the role (or not) of business education in the development of the ethical behavior of the business community, and proposals on how educators can attempt to change the ethical behavior or awareness of future members of the business community. In accounting education, this category of the literature includes surveys of the state of ethics education at accounting programs, studies of the development of ethical awareness and/or reasoning of accounting students and professionals, and debate over the best approach to incorporation of ethics into accounting education (e.g. separate ethics course versus integration into many accounting/business courses). The common theme in the accounting literature is the acknowledgment that accounting programs should provide at least some coverage of ethics in their accounting programs. Accounting academics and accounting professionals may not always agree on the nature, content, and presentation of ethics topics, but they do agree future accounting professionals should demonstrate knowledge of their ethical responsibilities.

The other broad category of the literature on ethics in education examines the training and behavior of academics. This literature assesses the ethical responsibilities of academics as educators, researchers, administrators, and members of society. Studies in this literature have assessed the dimensions of the development of ethical behavior of academics and debated the need and appropriate methods for ethics education. The literature on the ethics of accounting academics includes assessment of ethical development and behavior by accounting professors and administrators, and proposals for ethical codes of conduct for accounting academics and ethical training for accounting doctoral students and professors.

The ethical issues of individual choice and institutional structure are linked. Accordingly, institutional factors can have a profound effect on the choices made by individual faculty members. Evidence suggests that accounting faculty members might need to substantially improve their decision making about ethical situations. In 1989, the American Accounting Association (AAA) established a policy that encouraged authors to provide access to their data to others and include a statement about data availability. One purpose of this policy was to permit research replication to deter or detect research misconduct. Choo, Huang, Leong, and Wagner (1993) found that only 39% of the *Accounting Review* authors contacted responded in a positive manner to a request for their data (cited in Loeb & Merino, 2000, p. 299). Was detection of research misconduct a factor influencing the response rate? Evidence suggests the answer is "Yes" as Bailey, Hasselback, and Karcher (2001, p. 26) estimated that the actual percentage of seriously tainted articles in the top 30 accounting journals was approximately 4%. This finding is supported by Meyer and McMahon (2004), who, after conducting a survey of experienced and novice accounting researchers on ethical research conduct, concluded that

> There are [also] a number of behaviors where the perceived degree of occurrence is rather high in spite of the fact that the behavior is considered rather inappropriate. The degree of firsthand knowledge of those behaviors rated as inappropriate is rather disturbing (p. 440).

The issue of ethical behavior is not restricted to accounting faculty. A study of accounting administrators' attitudes toward ethically ambiguous fundraising situations demonstrated "… substantial variation in the decisions the administrators would make …" (Carver, Hirsch, & Strickland, 1993, p. 316).

Types of Ethical Codes

Researchers examining ethical codes have identified different types of ethical codes defined largely in terms of the autonomy given to individuals in their identification of ethical behavior. At one end of the spectrum are value-based codes that provide broad principles designed to guide actions of individuals (Robin, Giallourakis, David, & Moritz, 1989, p. 72). Individuals draw on these codes for inspiration in their individual analysis and resolution of ethical dilemmas (Pelfrey & Peacock, 1991, p. 14; Farrell, Cobbin, & Farrell, 2002, p. 156). Such codes are generally equated in the literature with codes of ethics, value statements, and credos (Fisher, 2001, p. 146; Farrell & Cobbin, 2000, p. 181; Murphy, 1995, pp. 728–732).

The other end of the autonomy spectrum is represented by rule-based, detailed and prescriptive codes that aim to provide ethical behavior for every possible situation. Codes of this nature remove the need for an individual's analysis and resolution of ethical dilemmas by specifying correct responses (Pelfrey & Peacock, 1991, p. 15). Individuals are expected to obey the rules; therefore, codes of this nature may contain enforcement sanctions and disciplinary processes (Farrell et al., 2002, p. 155). The literature equates such an approach with codes of conduct (Fisher, 2001, p. 145; Farrell & Cobbin, 2000, p. 182; Murphy, 1995, pp. 728–732). In practice, many ethical codes fall somewhere between these two ends of the spectrum (Pelfrey & Peacock, 1991, p. 15).

Arguments Concerning Accounting Academic Unit Codes of Ethics

A number of authors have presented the case for the establishment of a code of ethics for accounting academics (see, e.g. Loeb, 1990, 1994; Mintz, 1993; Crain & Carruth, 1992; Hillison & Williams, 1983; Keys & Hendricks, 1984). Ethical code benefits are enhanced for individuals that are given a high degree of autonomy and placed in situations where it is difficult to monitor their behavior, as would be the case for accounting faculty (Farrell et al., 2002, p. 159). Loeb (1990, pp. 125–126, 1994, pp. 194–195) provides an overview of the debate regarding the need for a code of ethics for accounting academics. Arguments discussed by Loeb and others for a code include:

- guidance in solving ethical dilemmas faced by accounting educators;
- setting societal expectations;
- education of accounting doctoral students;
- enhancement of accounting educators' reputation, and provision of solutions when ethical opinions differ between individuals;
- education/instruction aimed at encouraging individuals to understand and accept ethical behavior;
- enhancing public trust and accountability (Farrell et al., 2002, p. 156; Frankel, 1989, p. 111);
- fostering of group solidarity and common purpose (Frankel, 1989, p. 111);
- motivating individuals to behave according to socially defined virtues;
- empowering individuals to act in accordance with social interests rather than just organizational or self-interest (Fisher, 2001, p. 146); and
- increase in organizational efficiency and reduction of uncertainty when individuals agree on a common set of ethical values.

An argument for having an accounting faculty ethical code is that faculties are mobile and change institutions. "… A new faculty member cannot assume that what was acceptable at one's former institution will be acceptable at another institution." A departmental ethical code can be the interaction between the institution and the departmental members that helps define the "shared reality" of beliefs, behavior, and professionalism (Bruhn et al., p. 465).

In response to demands for an accounting academic ethical code, the International Association For Accounting Education and Research published, in 2002, a "Global Code of Ethics For Accounting Educators," which is reproduced in Exhibit 1. This value-based code contains 32 distinct principles and provides a broad benchmark for evaluating accounting faculty ethical codes.

Arguments against a separate accounting faculty ethical code include:

- a belief that accounting academics are no different than academics in other disciplines;
- a lack of need because accounting academics are required to follow other codes of ethics (e.g., university and/or professional codes such as the AICPA code);
- difficulty in the formulation of the code due to differences in opinion on the content of the code; and
- doubts regarding the effectiveness of an ethical code (Loeb, 1994, pp. 193–194).

Accounting is a profession that views itself on par with the legal and medical professions. Accordingly, it is appropriate to see what academic ethical expectations are for those professions.

When we look at the legal profession we find the 1986 American Bar Association's (ABA) Commission on Professionalism commenting "the law school experience provides the student's first exposure to the profession and … professors inevitably serve as important role models for students, … the highest standards of ethics and professionalism should be adhered to within law schools" (quoted in second paragraph Association of American Law Schools, 1989). To further this goal, the Association of American Law Schools formulated a *Statement of Good Practices By Law Professors In Discharge of Their Ethical and Professional Responsibilities* which addresses responsibilities (1) to students, (2) as scholars, (3) to colleagues, (4) to their school and university at which they teach, and (5) to the bar and general public (Association of American Law Schools, 1989).

Exhibit 1. Global Code of Ethics for Accounting Educators*.

The International Association for Accounting Education and Research (IAAER)

Preamble

The association is committed to promoting excellence in accounting education and research on a worldwide basis. It aspires to maximize the contribution of accounting academics to the development and maintenance of high quality, globally recognized standards of accounting education, research, and practice. Individual educators are leaders dedicated to and engaged in high-quality teaching and research in accounting.

Responsibilities in Accounting Education

Educational responsibilities

- Accounting educators accept responsibility for competent, inspirational, scholarly instruction.
- Respect for the integrity and teaching scholarship of academic colleagues requires unbiased, cooperative interaction with colleagues at home and abroad.
- Educational responsibility requires maintaining basic principles of teaching and collegial evaluation standards.

Basic principles of teaching

- Teaching and a concern for student learning play a central role for the accounting educator. Teaching scholarship deserves evaluation and reward.
- Rewards for and improvements in teaching demand peer evaluation, collegial criticism, and the capability of addressing problem solving as a scholar. Teaching scholarship is open to use and review by one's peers.
- Professional ethics should pervade the teaching of accounting.
- Proper counsel of students is integral to effective teaching.

Tenure and promotion evaluation standards for accounting educators

- Accounting education administrators should clearly explain the major criteria for evaluating accounting educators for promotion and tenure.
- Tenure evaluators/promotion committees should apply criteria consistently. The evaluation process should provide guidance for the future.
- Institutional evaluators should provide institutional policy on tenure and promotion to outside reviewers.
- Outside reviewers should evaluate the teaching, research, and service record with consistency and freedom from bias. A reviewer must inform an institution of a conflict of interest.

Exhibit 1. *(Continued)*

Responsibilities in Academic Research

Responsibilities in the research mission
- The profession's research mission requires that accounting educators perform and report research designed to enhance the quality of accounting education and practice.
- When conducting research, accounting educators must maintain a high level of professional performance and frame of mind.
- The review and publishing of research require a professional attitude in reporting and evaluation of research.

Research performance
- Accounting educators must give proper credit to intellectual property.
- Accounting researchers and writers must maintain originality in their work. Research experiments and studies require objectivity, honesty and accuracy in reporting, and due diligence.
- Findings of plagiarism must be reported to the editor, publisher, and employer.
- Where necessary and appropriate, the confidentiality of sources including company and individual identification should be maintained.

Research review and journal policies
- Accounting journal editors and reviewers must assure an unbiased, objective, scholarly assessment of works submitted for publication or presentation.
- A research reviewer has a duty to disclose conflicts of interest to the editor or reviewing board or committee.
- Accounting educators serving as journal editors and reviewing committee chairs must specify the requirements and procedures for acceptance to the submitting researcher.
- Research reviewers should be positive and respectful in communicating the results of a review.

Responsibilities to the Accounting Profession

Professional responsibilities
- The accounting educator has a dual responsibility to the accounting practice profession and to the accounting academic community.
- Professional responsibilities include maintaining professional bearing and developing students and the profession.
- Accounting educators serve the academy, the profession, and the community.

Professional character
- The accounting educator must maintain competence, integrity, and objectivity in the classroom and in the professional community.
- Further, the accounting educator must be honest, trustworthy, and fair, and must avoid harm to others. This includes honoring confidentiality and respect for the privacy of others.

Professional development

- Accounting educators must seek continually to maintain and improve their professional knowledge, skills, and competence.
- Teachers and researchers must continually update their expertise for new or enhanced teaching and research methodologies.

Professional service

- Accounting educators should participate in university leadership and in the international academy.
- Accepting roles on committees and boards and as officers or executives for professional or academic organizations requires a desire and effort to fulfill the specific committee, board, officer, or executive duties as set forth by the organization and its management. Accounting educators should refuse assignments when contingencies preclude completing the service responsibly.
- Accounting educators should serve their community in a professional manner.

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Within the medical profession, the American Psychological Association (APA) has a Code of Conduct with 89 rules! This code has a section titled "Education and Training" (seven rules) and a section titled "Research and Publication" (15 rules). The Research and Publication section is explicit to the point of having a rule which states that "Except under exceptional circumstances, a student is listed as principal author on any multiple-authored article that is substantially based on the student's doctoral dissertation" (American Psychological Association, 2003, *8.12*). The contents of these rules clearly indicate that the psychologists' profession-wide code of ethics was intended to cover academic members and provides explicit guidance for those members.

Loeb (1994, pp. 193–194) re-iterated his earlier call for the establishment of a code of ethics by the AAA and presented data aimed at answering in his view the most significant argument against such a code – the claim that many accounting academics are subject to other codes of ethics. An analysis of the stated professional affiliations of a sample of the faculty at U.S. accounting programs showed that nearly half of the faculties listed in Hasselback were neither CPAs nor CAs (chartered accountants). Interestingly, Engle and Smith (1990, p. 16) found some limited evidence that non-CPA accounting educators viewed involvement with a list of questionable ethical activities as more unethical than their CPA counterparts.

Mintz (1993) discussed the applicability of the AICPA Code of Conduct to accounting academics in light of the "varied and complex relationships encountered in academe" (p. 35). Although he illustrated the application of Code of Conduct rules on Integrity and Objectivity (Rule 102), General Standards (Rule 201) and Acts Discreditable (Rule 501) to AICPA members acting as educators, Mintz also acknowledged that a significant number of accounting academics are not members of the AICPA and bound by its rules. Mintz also discussed the benefits and implementation issues of a code of ethics for academic accountants. Potential benefits include;

(1) a framework for resolution of ethical dilemmas,
(2) standards for acceptable behavior for new faculty and doctoral students,
(3) legitimacy and increased stature for accounting faculty teaching ethics to accounting students, and
(4) a code of ethics applicable to all accounting faculty regardless of professional qualifications.

We believe that the AICPA Code of Professional Conduct is inadequate for accounting educators when compared to ethical codes adopted by other

professions. For example, the AICPA Code within its 11 individual rules for professional conduct only addresses an academic member's professional responsibility in one interpretation of its rule on Integrity and Objectivity (ET 102-5, *Applicability of rule 102 to members performing educational services*). This rule defined faculty teaching, research, and scholarship as conducting professional services and therefore requires members to conduct these services with objectivity and integrity, free of conflicts of interest, not knowingly misrepresenting facts, and without subordination of judgment to others (ET Section 102.06).

Academia's Response to Calls for an Accounting Academic Code of Ethics

Borkowski and Gaffney (1995, p. 4) surveyed 193 U.S. accounting faculty at both doctoral and non-doctoral institutions for their opinions on the need for an academic code of ethics, the effectiveness of an academic code and the ethical problems facing accounting faculty. The respondents were evenly split on the need for the code of ethics with 50% saying "Yes" and 50% saying "No" to the question, "Is a Code of Ethics Needed for Accounting Academics?"(Borkowski & Gaffney, 1995, p. 7). Of the accounting faculty favoring a code, a small majority preferred voluntary to mandatory enforcement of the code (28% versus 22% of faculty surveyed). Overall, the accounting faculty surveyed believed that an academic code would be most effective for teaching doctoral students and raising the stature of the accounting academia. The respondents rated inattention to teaching and students, research fraud and plagiarism, and conflict between teaching and consulting as the most important ethical problems faced by accounting academics.

The Borkowski and Gaffney responses for accounting faculty at doctoral granting institutions did not concur with those of their academic colleagues at other accounting programs. The accounting faculty at doctoral granting institutions were more unfavorable about the need for a code (62% responded No, compared to 50% for all faculty surveyed and 45% for faculty at universities without doctoral programs). Significant support for an academic code came from faculty who were untenured, non-Ph.D., or assistant professors. Although still the top choice, confidence in the effectiveness of a code as a teaching tool for doctoral students was significantly less among the faculty at Ph.D. granting universities. Accounting faculty in Ph.D. programs evaluated the importance of ethical problems related to research plagiarism/fraud and conflicts between teaching and consulting lower than other faculty surveyed. Borkowski and Gaffney (1995, p. 14) concluded by questioning the need for a specialized code of ethics and

calling for further research on the specific ethical issues facing accounting academics as well as ways to lessen their incidence.

The AAA has not issued a rule-based, detailed prescriptive code of ethics but it does have a value-based ''Statement of Responsibilities'' sponsored by the AAA Professionalism and Ethics Committee (see Exhibit 2). The Preamble states,

> The American Accounting Association recognizes its mission to be the 'premier forum for scholarly interchange in accounting.' The Association acknowledges that its members share a number of common values including the importance of integrity, objectivity, a sense of community, open communications, respect for others, high ethical values and behaviors, an increasingly global perspective and an obligation to serve important stakeholders, including the broader society within which we operate. This statement is an expression of the values we share and, while not intended to be enforceable, is designed to serve as a broad guide to the behavior we expect of each other.

The statement outlines members' responsibilities in areas of enhancement of learning, pursuit, and advancement of knowledge and service activities.

Some would argue that the current American Accounting Association *Statement of Responsibilities* is sufficient for accounting academia. However, some shortcomings of this statement include:

- It is not intended to be enforceable.
- It is very general in nature and, therefore, lacks specificity (Meyer & McMahon, 2004, p. 440).
- Many academics are not aware of its existence.

In 2002, the International Association for Accounting Education and Research (IAAER) released *A Global Code of Ethics for Accounting Educators* (see Exhibit 1). An IAAER Task Force consisting of international accounting educators developed the Code to address accounting educators' responsibilities in the areas of accounting education, academic research, and service to the accounting profession. The Code includes 32 distinct ethical principles. Announcing the Code, the IAAER President Belverd Needles, Jr., stated:

> This Global Code of Ethics is intended not only to raise the awareness of accounting academics in all countries to their responsibilities for setting examples of ethical behavior for their students and with colleagues, but also to specify what those standards of ethical conduct should be. We want these standards to be a focal point of discussion and for national and regional academic bodies to consider adopting them for their membership. (Needles, 2002, p. 1)

Exhibit 2. American Accounting Association Statement of Responsibilities*.

Sponsored by the AAA Professionalism and Ethics Committee

Preamble

The American Accounting Association recognizes its mission to be the "premier forum for scholarly interchange in accounting." The Association acknowledges that its members share a number of common values including the importance of integrity, objectivity, a sense of community, open communications, respect for others, high ethical values and behaviors, an increasingly global perspective, and an obligation to serve important stakeholders, including the broader society within which we operate. This statement is an expression of the values we share and, while not intended to be enforceable, is designed to serve as a broad guide to the behavior we expect of each other.

Each of us acknowledges our obligation to serve our academic institution or employer, and to adhere to standards of conduct those institutions may have established. However, we also acknowledge an obligation peculiar to our special role within the accounting profession to serve the larger society in which we live. That larger society includes a variety of stakeholders, including our students, our academic colleagues, our business associates, other professional associations, governmental interests, our local communities, and the business community at large.

The remainder of this Statement further explains the concepts as they pertain to Association members. It is written primarily in the context of an academic member of the Association who is actively involved in teaching, service, and research. However, the concepts are intended for all members of the Association. This Statement is a living document, and is subject to critique and revision to assure the shared values of the Association's members are clearly expressed.

Responsibilities

Enhancement of learning

Association members serve society by contributing to the development of its future leaders. Members accept the responsibilities implied by their position as teachers and mentors, including helping students and staff to develop those specific skills that will enable them to become contributing members of the profession and society, and helping them develop a foundation for lifelong learning. Members also recognize that they contribute to the development of students in more indirect ways such as

- Developing in students an appreciation for the importance of ethics and professionalism as well as technical expertise.
- Creating a fair and honest classroom environment.
- Insisting on excellence while simultaneously treating all individuals with dignity.
- Conducting academic, business, and professional affairs with integrity.

Exhibit 2. (*Continued*)

Pursuit and Advancement of Knowledge

Association members serve their broader constituency through scholarship including the discovery, application, and integration of ideas that enhance our understanding of accounting, business, human interaction with accounting measurements or business activities, and society. Members fulfill their scholarship obligations in ways that match their professional abilities, backgrounds, interests, and their institutions' specific mission. Some aspects of that obligation include

- Establishing and maintaining a scholarship agenda that is directed to important societal and professional needs and stretches the member's knowledge.
- Maintaining and strengthening scholarly competence, consistent with the requirements of each member's own research agenda.
- Accepting criticism of one's own work and providing objective and constructive criticism to colleagues.
- Publishing one's scholarship in ways that make the results available both to scholars and to a larger community.
- Encouraging and promoting a variety of scholarship approaches that result in quality work and contribute to the enhancement of scholarship and the public good.

Service Activities

Association members accept a responsibility to perform service to society, their institutions, their academic discipline, the profession, the business community, and the social community. The form of that service will vary depending on members' unique skills, passions, and background. Service is generally enhanced when Association members

- Seek out opportunities for service consistent with their institution's mission, the Association's mission, and with a recognition that members have a unique role to play within our society as independent, objective evaluators of accounting activities.
- Complete the service obligations with a commitment to excellence.
- Avoid conflicts of interest between the member's academic efforts, business interests, and service activities.

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To date, the IAAER ethical code appears to have been mainly disseminated via national accounting professional organizations, which are members of the International Federation of Accountants. For example, the AICPA has posted the IAAER ethics code on its website and the Accounting Association of Australia and New Zealand distributed the ethics code to its members via its newsletter. We consider the IAAER code to be an excellent option for benchmarking accounting academic unit ethical guidance because of the breadth of the ethical principles contained therein.

When we consider the level of professional educator, the American Association of University Professors (AAUP) has a *Statement on Professional Ethics* (available at http://www.aaup.org/statements/Redbook/Rbethics.htm). This statement outlines the responsibilities of membership of the academic profession in the broad areas of advancement of knowledge, encouragement of learning by students, common membership in the community of scholars, pursuit of effective teaching and scholarship, and obligations as citizens of society. The AAUP defers enforcement of ethical standards to the individual institution of higher learning. Some organizations have adopted the AAUP Code, for example, the Academic Senate for California Community Colleges adopted the AAUP Statement in 1987 and has recommended that its community colleges develop code of ethics for faculty and at a minimum adopt the AAUP Statement on Professional Ethics (Academic Senate for California Community Colleges, 2002).

METHODOLOGY

Since their role is to lead the academic accounting profession through the education of future accounting academics, accounting doctoral degree granting programs should also be leading in the area of ethics. Accordingly, we believe they were the most appropriate group to survey to see how accounting academics are currently meeting their responsibility to establish ethical expectations.

In late 2003/early 2004, we conducted a content analysis of the websites of 70 doctoral granting institutions in the U.S. to attempt to determine the existence of code of ethics applicable to accounting faculty. Our sample included websites for all accounting programs that have conferred at least one doctorate or concentration in accounting since 1997 according to Hasselback (2002, third preliminary page prior to page 1). Exhibit 3 provides a list of the institutions included in this analysis.

Exhibit 3. University Websites Examined.

Alabama	Nebraska
Arizona	North Carolina
Arizona State	North Texas
Arkansas	Northwestern
California-Berkeley	Ohio State
Case Western	Oklahoma
Carnegie Mellon	Oklahoma State
Chicago	Oregon
Colorado	Pennsylvania
Connecticut	Penn State
Cornell	Pittsburgh
Drexel	Purdue
Duke	Rochester
Florida	St. Louis
Florida State	South Carolina
George Washington	South Florida
Georgia	Southern California
Harvard	Southern Illinois
Illinois-Urbana Champaign	Stanford
Indiana	SUNY-Buffalo
Iowa	Syracuse
Kansas	Temple
Kent State	Tennessee
Kentucky	Texas-Arlington
Louisiana State	Texas-Austin
Louisiana Tech	Texas A&M
Maryland	Texas Tech
Massachusetts	Tulane
MIT	Utah
Memphis	Virginia Commonwealth
Michigan	Virginia Tech
Michigan State	University of Washington
Mississippi	Washington University
Mississippi State	Washington State
Missouri	Wisconsin

Our search and analysis was conducted according to a uniform set of procedures that specified search terms[1] and required collection of data on such aspects as level of code of ethics (university, college/school, department, and program), parties subject to the code(s) (faculty, administrators, staff, and students), and source of code of ethics within the institution (e.g., state, academic affairs, human resources, faculty senate, etc.). Wherever possible, the researchers obtained an electronic and/or printed

copy of codes of ethics identified on the institution's website for review and content analysis.

We recognize that our website survey would not identify ethical codes that are not discussed or published on university websites. To gather data about possible non-website published codes, we conducted a second survey in Fall 2004. We randomly sampled 24 of the 70 schools by telephoning the accounting program administrators. We believe this sample size was adequate to evaluate the small population. We asked each administrator whether their school had a code of ethics for accounting faculty and/or code of ethics for business faculty. If the administrator answered yes, we requested a copy of the code. The telephone survey revealed one additional ethical code, which was a College of Business Credo not published on either the accounting department or College websites. This means the telephone survey supports the conclusion that the accounting department website survey was accurate and did not miss a significant number of ethical codes.

RESULTS

Website Survey

One item we searched for was the presence [or absence] of any type of codes of conduct applicable to administrators, faculty, staff, and/or students. We found 163 codes of various types for the 70 schools we examined:

Code of conduct	46
Honor code	20
Academic integrity	14
Sexual harassment	68
Other	15
Total codes	163

All schools examined had at least one of the previous types of codes of conduct. However, if we exclude codes which apply *only* to administrators, staff, and/or students, only 86 codes remain which apply to faculty. The 86 faculty-related codes were comprised of 68 sexual harassment codes and 18 other codes, which are analyzed in Table 1.

No accounting program reported the existence of a code of ethics which applied to accounting faculty only. Thus, this research indicates that

Table 1. Results of Content Analysis of Websites.

	Number	Percentage
University-wide codes of ethics applicable to faculty excluding sexual harassment	18	25.7
Source of faculty code of ethics		
State	3	4.2
University	17*	24.2
College/School of Business (all of college)		
Code applicable to faculty	5	7.1
Code applicable to students	13	18.6
College/School of Business programs		
Code applicable to all programs	11	15.7
Code applicable to MBA program only	5**	7.1
School/Department of Accounting		
Code applicable to accounting students only	1	1.4
Code applicable to accounting faculty only	0	0.0

*Two universities had a state-issued code and an additional university-issued code.
**One university had a college code of ethics and a code of ethics for the MBA program.

accounting doctoral programs have not elected to develop separate accounting faculty ethical codes.

When we consider the five College/School of Business codes, which were applicable to faculty, three of these were student honor codes which related to faculty solely by requiring faculty to clarify their students' understanding of the student honor code. Only two faculty codes at the College/School of Business level provided comprehensive ethical expectations regarding accounting faculty. These two ethical codes were found at the University of Kansas and the University of Oregon.

The previous two comprehensive business school codes were compared to the 32 IAAER (2002) ethical standards listed in Exhibit 1. We found that the business school ethical code for the University of Kansas included 2 of the 32 IAAER (2002) ethical standards (6%), while the business school code for the University of Oregon included 9 of the 32 IAAER (2002) ethical

standards (28%). This suggests that there is a considerable gap between the IAAER suggested ethical code and the two business school ethical codes, which have been currently enacted.

Interestingly, the University of Kansas business school ethical code included the following three items which were not in the IAAER (2002) ethical standards:

1. *Facilitating academic misconduct*: Giving or attempting to help another commit an act of academic misconduct, including failing to notify students of what constitutes academic misconduct.
2. *Tampering with records*: Interfering with, altering, or attempting to alter, university records for the purpose of falsely changing the original information.
3. *Behavioral misconduct*: Sexual harassment, discrimination, or instructing while impaired by alcohol, illegal drugs.

Telephone Interviews

As part of our telephone survey we also asked the accounting administrators whether they perceived any type of need for a separate accounting department faculty ethical code. To help summarize these responses, we decided to judgmentally classify them into three categories.

Administrator responses categorized as "No Perceived Need For Separate Ethical Code" included:

- "I need to think about this,"
- "I am not aware of abuses,"
- "No real need,"
- "No perceived need," and
- "Too busy with other things."

Administrator responses categorized as "Rely On Higher (University or College) Level Code" included:

- "Surprised at need for one since faculty under university code,"
- "University level code is sufficient. Accounting faculty not different from other professors in professional responsibilities,"
- "Have discussed need for accounting faculty code at college level but university is working on code so we will wait,"
- "Reliance on university faculty handbook," and
- "Wait and see how development of college code proceeds."

Administrators responses categorized as "Other" included:

- "I am not familiar with university code,"
- "Aware of cases where one needed through annual reports and discussion with committee chairs. Would prefer one at college level,"
- "Our Dean is asking faculty to share their ethical issues with students," and
- "No discussion among faculty but I think it could be useful and have value."

LIMITATIONS

One limitation of this research is that we searched for materials publicized on the university websites. Our website search was conducted through various website search engines and from a manual review of websites. It is possible that there were website published ethical codes which these search procedures missed. However, results of the telephone survey suggest that the number of missed ethical codes was minimal.

It is also possible that individual schools may have ethical codes published in media other than university websites and which were not thought of by the accounting program administrators contacted via telephone. For example, many universities have faculty handbooks containing some ethical provisions, which may not be available on university websites or thought of by accounting program administrators contacted via telephone.

CONCLUSIONS

Current AACSB accreditation eligibility standards state, "The accounting academic unit must establish expectations for ethical behavior by administrators, faculty, and students" (AACSB, 2005, p. 5). Accounting academic units can comply with this standard by adopting one of the following approaches:

- Establishing a separate ethical code for the accounting academic unit;
- Reliance on a separate ethical code established for the business school; or
- Reliance on ethical codes which may exist at other places, such as a university code or faculty handbook.

National surveys of U.S. accounting Ph.D. programs revealed that no accounting programs had taken the first approach and established a separate accounting faculty ethical code. The surveys found that only 2 of the

70 programs surveyed had comprehensive faculty ethical codes at the College/School of Business level. A review of these two published ethical codes revealed that they appeared to cover a maximum of only 28% of the ethical areas identified in the comprehensive *Global Code of Ethics for Accounting Educators* published by the IAAER (2002). All programs surveyed had university level codes. Thus, this research reveals that, currently, almost all U.S. accounting Ph.D. programs have chosen to rely on ethical codes that exist at the university level.

We believe that accounting academic programs should, at a minimum, evaluate the adequacy of their existing ethical guidance using either a sample of peer institutions or a comprehensive code, such as the IAAER (2002) *Global Code of Ethics for Accounting Educators*, as a benchmark. This evaluation may indicate that existing ethical guidance is adequate and properly communicated. However, if this evaluation reveals serious shortcomings in either scope or communication then we believe, as does AACSB International, that consideration should be given to establishing a separate ethical code of conduct for accounting faculty. If a decision to proceed toward a separate ethical code is made, then accounting academic units do not need to start with a blank piece of paper. It would be advantageous to adopt by reference, portions of their university or business school ethical codes as part of the accounting academic unit ethical code. The accounting unit would then only need to develop the additional rules or guidance needed to fill in perceived gaps. This approach would have the advantage of conforming the accounting unit's code to higher authority codes. It would also mean that the academic unit could focus discussion primarily on areas where they believe they might need to supplement the other codes. The dialogue about adopting an ethical code will allow faculty to identify shared values and as well as areas where they have differences. Further examination and dialogue about areas of difference could be beneficial in resolving disagreements or other sources of friction within accounting academic units and with other components of the university or stakeholders. Adoption of a code might also raise the level of conduct in accounting academic units and help avoid future negative publicity.

Evaluation of the adequacy of existing ethical guidance is just a first step. As in the corporate world, ethics in academia must permeate daily decision making and there must be accountability for violators. Brooks (2004, p. 14) comments about this step:

> Not content to encourage the use of ethics just through a code of conduct, leading-edge corporations sought ways to inculcate ethics into their corporate culture to foster specific considerations of ethical conduct in operating decisions, in strategic decision making, and in crisis management practices.

We should not be doing any less in accounting academia. In light of the recent business scandals involving ethics, calls for reforms in ethical training of accounting students and professionals, and AACSB accreditation standards, accounting faculty might benefit from a serious dialogue about appropriate ethical expectations for accounting academics and accounting programs.

NOTES

1. Search terms used: code and ethics, ethics, honor and code, code and conduct, student behavior, sexual harassment, ethics policies, and behavior policies. If a website did not provide a search engine, the researchers examined the individual web pages of the university, college/school, and accounting department/programs.

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ETHICS OF CARE AND DECISIONS OF FINANCIAL STATEMENT PREPARERS TO MANAGE EARNINGS

Randall Rentfro and Karen L. Hooks

ABSTRACT

Agency theory would predict the self-interested behavior of corporate managers and financial statement preparers seen in recent accounting scandals. Yet, despite an environment replete with incentives to manage earnings, many preparers do not act in a self-interested manner. To better understand why preparers behave in different ways, this study examines the reporting decisions of 145 financial statement preparers in U.S. corporations in an experiment that manipulates both the motivation and the ability to manage earnings. The case setting emphasizes a personal relationship, which introduces the possibility that preparers will behave differently due to differences in moral orientation. Preparers using an ethic of rights orientation, which is aligned with agency theory, would be expected to engage in self-interested behavior. Those using an ethic of care orientation would be expected to act in ways that enhance the relationship.

In this study, female preparers responded differently than their male counterparts in the presence of agency theory's moral hazard conditions. When given the motivation and ability to manage earnings, the study's female preparers made more conservative reporting decisions than when

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these conditions were not present. This behavior is inconsistent with agency theory predictions and suggests that the females may have been acting to protect the relationship, which would be consistent with an ethic of care orientation. Males, however, responded as agency theory predicts.

The study's results support the extension of agency theory to include factors related to the agent's ethics. The findings also suggest that an understudied theory, the ethics of care, may be important to gender-related differences in decision processes and should be the object of further study.

Agency theory's moral hazard construct predicts that when agents possess private information and have an incentive to shirk, the agents will engage in short term, economically maximizing, self-interested behavior (Eisenhardt, 1989, p. 61). Behavior described by Federal Reserve Board Chairman Alan Greenspan during testimony before the United States Senate Committee on Banking, Housing and Urban Affairs is consistent with that which would be predicted by agency theory:

> An infectious greed seemed to grip much of business community .... As a result, the highly desirable spread of shareholding and options among business managers perversely created incentives to artificially inflate reported earnings in order to keep stock prices high and rising .... The incentives they created overcame the good judgment of too many corporate managers (Federal Reserve Board, 2002).

While the self-interested behavior has been demonstrated by the financial reporting abuses of managers at Enron, WorldCom and other corporations, not all managers and financial statement preparers facing similar situations and incentives have chosen to manage earnings. This study considers these differing behaviors of financial statement preparers. Do personal characteristics influence the decisions of preparers to manage earnings? And, further, do men and women make different decisions when an important personal relationship is a part of the fact pattern involved in the decision? The fundamental purpose of this paper is to explore the behavior of financial statement preparers, introducing gender as an observable variable, which may be associated with differences in behavior.

Bohren (1998, p. 753) challenges the agency theory assumptions that all individual agents are indifferent between making honest and dishonest decisions. Similarly, Noreen (1988, p. 368) argues that agency theory inappropriately assumes unconstrained opportunism on the part of the agent. Noreen notes that while research has shown examples of unethical opportunism, many examples of other behaviors also exist. This observation is relevant to the point of our study.

In addition to basing this study on Bohren's (1998) and Noreen's (1988) call for extension of the classical agency model, we rely on moral intensity theory (Jones, 1991) and consideration of the moral orientation of the individual. Moral intensity theory asserts that in order for a moral decision framework to be used by a decision maker, he or she must recognize that the decision includes moral components (Jones, 1991, p. 380). This recognition of moral components is more likely to occur when the issue has a high level of moral intensity for the decision maker (Jones, 1991, p. 380). Several variables that increase moral intensity, such as close proximity of those affected by the outcome to the decision maker and magnitude or concentration of the impact of the decision on those people affected, are associated with personal relationships (Jones, 1991, p. 374).

One aim of this study is adding to the literature challenging the agency theory assumption of universal short term, economically maximizing, self-interested behavior decisions by agents. We explore this by introducing personal relationships as an important component of the fact pattern underlying a decision. We propose that the relationship component will heighten the moral intensity of the decision for those decision makers grounded in a care ethic orientation, thus causing a decision framework other than that of agency theory to be employed.

Ethics of care theory suggests that because they are more likely to have a care orientation, women are, in general, more sensitive than men to relationship issues. Therefore, personal interactions and impact on others rather than adherence to rules will influence their decisions (Tronto, 1993, p. 79). Reiter (1997, p. 204) states, "Acknowledgement and effective management of relationships is at the core of the ethics of care". The case used in this study includes an "important relationship" in the fact pattern underlying the financial reporting decision made by participants. Women are expected to be more sensitive than men to the relationship issues of the case, more aware of the moral aspects of the decision based on a sense of heightened moral intensity, and more likely than men to choose the decision alternative whose outcome would nurture the important relationship; in this case, the decision to refrain from managing earnings upward. The study's findings support the expected outcome.

This study contributes to the accounting literature by identifying gender as a personal characteristic associated with differences in the decisions of financial statement preparers, and proposing moral intensity and ethical orientation as theoretical underpinnings for the finding. The study also contributes to agency literature by presenting a situation in which agency theory predictions of behavior do not hold true for all the participants. The

results add to the earnings management literature by displaying demographic factors and their association with observed differences in earnings management behaviors. Finally, the study is based on the decisions of a sample of financial statement preparers, a realistic population that is infrequently the object of accounting study.

REVIEW OF PRIOR LITERATURE AND DEVELOPMENT OF HYPOTHESES

Earnings Management

Healy and Wahlen (1999) define earnings management as follows:

> Earnings management occurs when managers use judgment in financial reporting and in structuring transactions to alter financial reports to either mislead some stakeholders about the underlying economic performance of the company or to influence contractual outcomes that depend on reported accounting numbers (p. 368).

This study draws upon this definition by using a case in which the relevant accounting standard requires financial statement preparers to make numerous, important professional judgments or decisions in order to apply the standard. Thus, the standard provides opportunities for the preparers to manage earnings. The case in the study also provides participants with the motivation to manage earnings to their advantage through the existence of a profit-sharing plan. Prior research confirms that income-based compensation contracts, such as used in this study, motivate managers to manage earnings (Healy & Wahlen, 1999, p. 375).

Agency Theory

Agency theory also informs this study. When the economic interests of managers, acting as agents, differ from those of the stockholders or principals, managers have an incentive to shirk (Baiman, 1982, p. 342). The incentive to shirk is one of the two conditions that comprise the moral hazard construct in agency theory (Tuttle, Harrell, & Harrison, 1997, p. 8). In the case used in this study, the incentive to shirk – or manage earnings to the financial statement preparer's advantage – is presented through the existence of a profit-sharing plan. If the preparer manages earnings to his or her advantage, the company's earnings will be higher, and the profit-sharing plan will provide more compensation to the preparer.

When the incentive to shirk is combined with privately held information, which effectively provides the agent with the ability to shirk, moral hazard is said to exist (Tuttle et al., 1997, p. 8). Agency theory predicts that in such cases, agents or decision makers will engage in short term, economically self-interested behavior, known as shirking (Eisenhardt, 1989, p. 61). This study presents preparers with a moral hazard condition created by (1) the motivation to manage earnings for the purpose of increasing compensation from a profit-sharing plan and (2) the ability to manage earnings as a result of having private information unknown to the decision maker's superior.

Moral Intensity

Rutledge and Karim (1999, pp. 179–180) and Tuttle et al. (1997, p. 22) provide empirical evidence that ethical considerations may moderate agents' self-interested behavior under moral hazard conditions. Rutledge and Karim (1999, p. 181) find that moral reasoning levels influence managers' project-evaluation decisions. Tuttle et al. (1997, p. 22) find that information systems professionals' ethics affect decisions to implement information systems. As described above, this study's case setting includes conditions of agency theory's moral hazard. We add the component of an important personal relationship to the case, to examine moral intensity and ethical orientation as possible moderating variables in the presence of moral hazard.

The effect of moral intensity on ethical decision making is outlined in Jones (1991). Jones (1991) expanded Rest's (1979, 1986, 1994) Model of Ethical Action to include characteristics of the moral issue, which Jones (1991) collectively calls moral intensity (p. 371). Although Rest's (1979, 1986, 1994) model has been adapted in a variety of ways, it begins with a decision issue that has moral components (Jones, 1991, p. 370). According to Hooks and Tyson (1995), "A moral issue, as used in Jones (1991) model, is one that will result in an action or decision that will affect others and one in which the decision maker has a choice. The action or decision must result in consequences for others" (p. 269). The decision maker recognizes the issue as being one with moral components, and then must make a judgment regarding the moral issue. Next a behavior decision is made, and the actor may choose a "moral" or other behavior. The last step is to engage in the selected behavior.

Each step of the process is affected by the intensity of the moral issue. Issue-contingent factors (Jones, 1991, p. 372) that will affect each step of the decision process include magnitude of the consequences, social consensus, probability of effect, temporal immediacy, proximity and concentration of effect. In other words, significance of the good or harm, agreement among

the decision maker's reference group, likelihood of the outcome, chronological nearness of the outcome, closeness of those affected to the decision maker and severity of the consequence for the people affected all impact the intensity with which the decision maker feels the moral issue.

For purposes of this study, we focus on issue-contingent factors that can be theorized to be important to a relationship. Many of the factors fit this characterization. For example, if the person affected by the decision is in close proximity to the decision maker and will experience clear consequences, then the decision will have effects on a relationship. This is consistent with Reiter's (1997) description of an ethics of care response in which the decision maker views "the self and others as interdependent with relationships created and sustained by attention and response" (p. 303). In addition to personal relationships, if the outcome of the decision has a questionable likelihood of actually occurring, or the outcome event is in the distant future, the ethical issue will have a lesser intensity and the decision maker will be less concerned about impacts on a personal relationship.

Rest (1994, p. 22) notes that a limitation of much research is the inability to determine whether the decision with which a person is faced is perceived as a moral issue, and if so, to what extent. This study does not rely upon creating a "moral dilemma". We present an accounting decision with an important personal relationship as a part of the case fact pattern. We assume that a heightened moral intensity will affect those study participants who are sensitive to the relationship consequences of the decision. We recognized that we were taking a risk in the research design by making this assumption. However, our results indicate that the assumption was justified.

All stages of the Model of Ethical Action and the intensity of the issue can be proposed to be affected by relationships. Beginning with the first step of recognizing a decision as one with ethical components, the interaction is clear. If a decision has an impact on others, it has ethical components. Therefore, someone more in tune with relationship effects will be more likely to recognize such a decision as being a moral one than a person who is unconcerned about relationships. Ethics of care orientation theory, discussed in the next section, clearly portrays a potential interaction between moral intensity issues and concern for relationships in decision making.

Ethics of Care

General understanding of the ethics of care has grown since its first introduction by Gilligan (1982) in *A Different Voice*. Tronto (1993, p. 79) describes the ethics of care as being based on responsibility and relationships. This

differs from the ethics of rights or ethic of justice that has been a long-standing benchmark used by Kohlberg (1969) and others. Reiter (1997), citing Tronto (1993), discussed the concept that ethics of care departs from the long-standing ethic of rights view that ethical decisions must be made from a detached and objective vantage. Reiter (1997) states that "the ideal state for professional judgment is a set of appropriately embedded relationships, rather than a mythic independence of mind" (p. 303). Brabeck (1993, p. 34) also distinguishes the ethics of care as being based on connections to others, with relationships being the primary consideration. Using this simple definition, a person grounding a decision based on a care orientation will be concerned about responsibility to others and hurting other people. In contrast, grounding a decision based on a rights orientation will focus on conflicts and bargaining, and concern for the autonomous and separate individual (Sichel, 1987, p. 322).

Ethics of care was first articulated in the feminist literature. Although results are mixed in the many studies addressing moral orientation, studies of physicians (for a review, see Self & Baldwin, 1994) and veterinary medicine students (for a review, see Self, Olivarez, & Baldwin, 1994) support the conclusion that women are more likely to base decisions on a care orientation, while men are more likely to use a justice orientation. This holds even though moral developments studies, which are grounded in justice ethics, often show either no gender difference or a higher moral development in women (Rest, 1994, pp. 14–15). Reiter (1997) proposes that a relationship-based approach to the world may reflect a moral maturity and an "ideal of concerned and caring adulthood" (p. 303). Traditionally, in the U.S. culture, ethics of rights has been elevated as the "appropriate" structure for business decisions, parallel with the assumptions of agency theory. "The autonomous and competitive characteristics of the rights and justice theories lead to the underlying assumptions of agency theory, that conflict and competition between owners and managers is the central theme of corporate life" (Reiter, 1997, p. 304). In this study, we challenge the assumption of the universal appropriateness and superiority of agency and ethic of rights as explanatory theories. We utilize a set of facts in which one of the concerns of the decision maker is maintaining a relationship, although a moral hazard opportunity is presented. Thus, one might say that two competing models are juxtaposed in the facts of the case. Moral hazard of agency theory proposes that an individual will act in a self-interested manner. Ethics of care orientation theory proposes that relationships are the grounding factor upon which women will base decisions. Although agency theory does not propose a gender predisposition, the alignment of agency theory and an ethic of rights or justice (which is the counterpoint to an ethic of care) raises

the possibility that the behavior of female decision makers will not be well explained by agency theory.

Demographics and Judgments

Empirical studies of the behavior of accountants provide mixed evidence that a number of demographic factors may influence accountants' judgments and decisions, particularly those that may have an ethical component. Elias (2002, pp. 114–119) finds that factors including age, experience, job title, education and income level are related to differences in accountants' perceptions of the acceptability of earnings management. Similarly, Rosenzweig and Fischer (1994, p. 31) find that accountants with more experience and at higher organizational rank are more tolerant of earnings management. Smith and Rogers (2000, p. 80) find that men and women assess ethics violations differently and that experience also influences these assessments. Radtke (2000, pp. 303–306) finds mixed evidence that gender is associated with ethically sensitive decisions made by accountants. Larkin (2000, p. 407) concludes that female internal auditors are better able than their male counterparts to identify ethical behavior and also finds that more experienced auditors tend to be more conservative in their ethical interpretations. Sims and Keenan (1998, p. 418) find that whistleblowing is significantly related to gender, but not organizational tenure, age or education. These findings require that we explore our subjects' responses for correlation between gender and age and experience and rank. Demographic variables correlating with gender are used as covariates in the study's analyses.

Hypotheses

Moral intensity and ethics of care orientation theories support the proposition that women will recognize moral implications of a decision that has an effect on a personal relationship and because of this may make different decisions from men. We expect personal relationship factors to moderate the effects of moral hazard conditions on female financial statement preparers as they make reporting decisions. Given this expectation, hypothesis one is as follows (stated in the alternative form):

> **H1.** When making reporting decisions that affect earnings, in the presence of a strong expected impact on relationships as a result of the decision, female financial statement preparers will respond differently to moral hazard conditions than male financial statement preparers.

The primary question of this study is presented in hypothesis one. However, to further explore the impact of relationships on decisions we also test the situation in which the decision maker has the ability to manage earnings through the possession of private information, without the obvious motivation of the profit-sharing plan. The purpose of this hypothesis is to address whether women may be more sensitive to the relationship condition than men in the normal course of business. Hypothesis two is:

> **H2.** When making reporting decisions that affect earnings, in the presence of a strong expected impact on relationships as a result of the decision, female financial statement preparers will respond differently to the ability to manage earnings through private information and information asymmetry than male financial statement preparers.

Lastly, we address the possibility of earnings management in the situation where a motivation exists, through the form of compensation from a profit-sharing plan, but the ability to manage earnings discretely does not exist. In this situation, the decision maker does not have private information, and any decision to manage earnings will be obvious and known to the decision maker's superior, with whom an important relationship exists.

> **H3.** When making reporting decisions that affect earnings, in the presence of a strong expected impact on relationships as a result of the decision, female financial statement preparers will respond differently to the motivation to manage earnings when private information does not exist than male financial statement preparers.

RESEARCH DESIGN AND METHODOLOGY

The Experiment

Using the moral hazard construct in agency theory as a guide, we designed an experiment to test whether financial statement preparers manage earnings when they have the motivation and ability to do so. In the experiment, participants are asked to assume the CFO role in a hypothetical company. The motivation to manage earnings is represented in the case by the presence of a profit-sharing plan that is a significant component of the CFO's compensation. The ability to manage earnings is represented by the presence of information known only by the CFO.

The case discusses a potential impairment of a long-lived asset and asks participants to state how likely they would be to recognize an impairment loss in the company's financial statements. To assist the participants in determining if a loss should be recognized, the case materials include a summary of the guidance in Statement of Financial Accounting Standards (FAS) No. 121, *Accounting for the impairment of Long-Lived Assets and for long-Lived Assets to be Disposed of* (FASB, 1995).[1] A decision to recognize the impairment loss will result in reduced earnings, while a decision to forgo recognizing the loss manages earnings upward.

The case also describes a significant relationship between the participant, who is instructed to take the role of a CFO, and the company's new CEO. The case states that the CFO would like to establish a good working relationship with the new CEO, and it also presents a self-interest motive for this relationship, stating that the CFO believes a good relationship will improve prospects for promotion. Two paragraphs of the five in the case discuss the new CEO, including statements that she is female, is a former CFO and is known to be highly ethical, well informed on accounting standards and insistent upon strict adherence to the standards. Finally, the case indicates that the current CFO, whose role the participant is taking, has been the company's CFO for five years, implying an employment situation that likely involves a number of personal relationships. Nothing in the case suggests any job dissatisfaction or desire to change jobs on the part of the CFO; the desire for a promotion was intended to imply that the CFO desires to stay with the company.

Development of Experimental Materials

As we developed the case, we had to identify a financial reporting issue for the participants to consider. Given Healy and Wahlen's (1999, p. 368) earnings management definition, it was important to choose an issue in which professional judgment could be used to manage earnings. Furthermore, we wanted an issue that would require a number of judgments or decision points so that participants would have many opportunities to manage earnings. After reviewing several accounting standards, we selected the impairment of a long-lived asset as a potential reporting issue and FAS No. 121 as the accounting standard to guide that reporting decision.

To verify that FAS No. 121 includes sufficient opportunities to manage earnings, we used a method developed by Mason and Gibbins (1991). The method identifies the number of instances in which professional judgment is required to apply accounting standards. This approach is consistent with

Brown (1999, p. 61), who notes that earnings management occurs when managers make choices, judgments and estimates within the bounds of GAAP to influence earnings. Brown (1999) further states that "the wider the range of choices, the more opportunity open to management teams to manage – some would say manipulate – reported earnings to their advantage" (p. 61). Consistent with Brown (1999), Mason and Gibbins' (1991) method produces a measure of the opportunities financial statement preparers have for managing earnings within the bounds of accounting standards.

We asked three accounting academics independent of the study to evaluate FAS No. 121 using the Mason and Gibbins (1991) method. The professors reviewed the standard and counted the number of instances in which FAS No. 121 requires the financial statement preparers to make a judgment. The average number of judgments identified by the panel was 28. This indicates that FAS No. 121 provides many opportunities for earnings management.

We then asked a second panel of four experts (consisting of auditors in practice and accounting academics) to review the instances of professional judgment identified by the previous panel. The second panel rated the relevance (using a 5-point scale with endpoints identified as 1 = very little relevance and 5 = very highly relevant) of each judgment to an overall decision that an asset is impaired. This procedure tests whether the judgments required by the standard are important. FAS No. 121 had 18 judgments that were rated as highly relevant to an asset impairment decision. Based on this, we determined that FAS No. 121 had several important decision points, which would allow financial statement preparers to manage earnings.

The case, which we developed specifically for the experiment, provides participants with (1) background information about a health care software company, including the relationship information described previously; (2) information about the long-lived asset impairment decision facing the CFO; and (3) a summary of FAS No. 121. Some bold face type was used to emphasize the relationship aspects of the case and information concerning the moral hazard conditions. In addition to the case materials, the experimental instrument included introductory instructions, scales for indicating the participant's reporting decision and a post-experiment questionnaire to collect demographic data and manipulation-check data.

An expert panel reviewed the case and identified which of the FAS No. 121 judgments required were represented in the case. A super-majority of the panel members agreed that the case includes 12 judgments required by FAS No. 121. All but one of the judgments were rated by panel members as highly relevant to the asset impairment decision. Therefore, we believe the case captures the essential elements of the FAS No. 121 decision-making process.

Participants

The study participants in the study are accountants who work in U.S. corporations and are or have been engaged in financial statement preparation. A total of 145 accountants participated in the study after being recruited through professional organizations and other means. Further information about the participants is included in the Results section.

Experimental Procedures

In order to test all three hypotheses, we randomly assigned participants to one of the four groups: (1) control, (2) motivation to manage earnings, (3) ability to manage earnings, and (4) a moral hazard.[2] We distributed the packet of experimental materials to the participants by mail. Follow-up procedures were used to improve response rates.

Participants assumed the role of the CFO of the software company. After reading the background information about the company, the participants read the description of the long-lived asset impairment decision facing the CFO and a summary of FAS No. 121. The participants then indicated their likelihood of reporting an impairment loss on the company's income statement for the current period. After making the reporting decision, the participants provided demographic and manipulation check data and returned the materials using a postage-paid return envelope.

Research Design

The study has two between-subjects factors: (1) motivation to manage earnings and (2) ability to manage earnings. The motivation to manage earnings factor has two levels represented by the presence or absence of a profit-sharing plan as a significant portion of the CFO's compensation. The ability to manage earnings factor has two levels represented by private or public information about future cash flows from the asset. In the private information condition, only the CFO is aware of the cash flow forecasts. In the public information condition, the CFO has shared the cash flow forecasts with the CEO.

Given the study's hypotheses, gender is included as an independent variable. The remaining demographic variables (age, experience and rank) are potential covariates. The dependent variable is the participants' likelihood of recording an impairment loss (using a 7-point scale with 1 = Definitely will NOT report and 7 = Definitely will report).

Design Choices and Limitations

As we designed the experiment, we made design choices intended to keep the experiment to a reasonable length. We were concerned that financial statement preparers would not participate if the experiment required more than 20 min to complete. Consequently, we chose not to administer additional instruments, which might have enhanced our understanding of the study's results.

Prior research suggests that gender may be related to differences in moral development[3] and risk preferences.[4] Consequently, an ideal design for this study would have included administering an instrument to measure the moral development of our participants and also using an instrument to measure our participants' risk preferences. We chose not to do so because these instruments would add considerable length to the experiment. This design choice is a limitation in our research. We cannot rule out differences in moral development or risk preferences as explanations for any differences in the behavior of males and females in our study. However, given the emphasis on personal relationships in our case setting, we believe our research design is appropriate as an early exploratory study examining whether moral orientation may explain differing behavior of male and female financial statement preparers.

RESULTS

We mailed materials to 276 accountants in corporations across the United States, and 145 accountants participated in the study, resulting in a 53% response rate. We used data from the post-experiment questionnaire to determine if the participants had experience in financial statement preparation. The questionnaire asked participants to indicate whether their major job responsibilities are or were in financial accounting and whether they have supervised the preparation of financial statements. We also asked participants to rate their familiarity with FAS No. 121 (using a 5-point scale with the endpoints identified as "not at all familiar" and "very familiar") and their comfort level in making the long-lived asset impairment decision in the case (using a 5-point scale with the endpoints identified as "not at all comfortable" and "very comfortable"). Based on the participants' responses to these questions, we determined that six participants were not financial statement preparers. Therefore, we excluded their responses from the statistical analysis.

The participants also responded to two manipulation-check questions. These questions tested whether the participants were aware of the CFO's compensation plan and whether the CFO has private information. The private information question also provided evidence of the participants' awareness of the issue of the relationship with the CEO. Twenty participants did not pass the manipulation checks, and we excluded their responses from the statistical analysis. Therefore, the study's results are based on the responses of the 119 financial statement preparers who passed the manipulation check questions. Of the 119 participants, 78 were males, and 41 were females. Nearly, 83% of the participants hold management-level positions of accounting manager/supervisor or higher (e.g., Controller, CFO and Vice President), and 70% of the participants have over 10 years of professional work experience. 57% of the participants work for manufacturing companies, and the remaining participants work in a variety of other industries including health care, construction, real estate, technology and entertainment.

Means and Variances

The means and variances of the long-lived asset impairment decisions are reported in Table 1.

Demographic Variable Correlations

The correlations between the demographic variables are reported in Table 2. Rank was not correlated with gender and was, therefore, excluded from further analyses. Experience and age were included as covariates in the analysis of variance procedures because both variables were correlated with gender.

ANCOVA and ANOVA Results

ANCOVA procedures revealed a significant interaction between the two moral hazard conditions (ability and motivation) and gender (see Table 3). In other words, preparers who had the ability and/or motivation to manage earnings made different impairment decisions than preparers in the control group. This suggests that earnings management was occurring. However, the interaction with gender indicates that female financial statement preparers were managing earnings in a different manner than their male counterparts.

To better understand how the decisions of females and males differed, we ran separate ANOVAs for each gender (see Tables 4 and 5). The results continue to show a statistically significant interaction between ability and

Table 1. Long-Lived Asset Impairment Decision Means and Variances (1 = Definitely will Not Report Impairment Loss …, 7 = Definitely will Report Impairment Loss).

	N	Means	Variances
Experimental group			
All participants	119	2.824	3.519
Control	30	2.933	3.099
Ability to manage earnings	31	2.548	3.323
Motivation to manage earnings	25	3.200	3.333
Moral hazard	33	2.697	4.342
Rank			
President/vice president	16	3.125	4.517
CFO	15	2.467	2.124
Controller	34	2.676	3.256
Manager/supervisor	32	2.656	3.200
Senior/staff	22	3.318	4.799
Years of experience			
5 or less	10	3.500	4.944
6–10	26	2.846	3.415
11–15	24	2.708	3.085
16 or more	59	2.746	3.607
Gender			
Male	78	2.692	2.995
Female	41	3.073	4.520
Age			
30 or less	19	3.474	4.819
31–40	45	2.577	2.749
41–50	35	2.829	3.323
50 or more	20	2.750	4.408

Table 2. Demographic Variable Correlation Matrix.

	Gender	Experience	Age	Rank
Gender	1.000	**–0.286***	**–0.247***	0.153
Experience	**–0.286***	1.000	**0.727***	**–0.384***
Age	**–0.247***	**0.727***	1.000	**–0.290***
Rank	0.153	**–0.384***	**–0.290***	1.000

*Significant at 0.01 level.

Table 3. Analysis of Covariance Long-Lived Asset Impairment Decisions All Preparers ($n = 119$).

Effect	Df	Type III SS	Mean Square	F-value	Prob > F
Motivation to manage earnings	1	2.749	2.749	0.818	0.368
Ability to manage earnings	1	1.380	1.380	0.411	0.523
Gender	1	2.318	2.318	0.690	0.408
Age	1	0.028	0.028	0.008	0.928
Experience	1	0.182	0.182	0.054	0.816
Motivation × ability	1	3.835	3.835	1.141	0.288
Gender × motivation	1	2.823	2.823	0.840	0.361
Gender × ability	1	5.281	5.281	1.572	0.213
Gender × motivation × ability	1	30.228	30.228	8.996	**0.003**
Error	109	366.239	3.360	–	–

Table 4. Analysis of Variance Long-Lived Asset Impairment Decisions Female Financial Statement Preparers Only ($n = 41$).

Effect	Df	Type III SS	Mean Square	F-value	Prob > F
Motivation to manage earnings	1	4.254	4.254	1.01	0.322
Ability to manage earnings	1	0.0375	0.0375	0.09	0.768
Motivation × ability	1	21.838	21.838	5.19	**0.029**
Error	37	180.781	180.781	–	–

Table 5. Analysis of Variance of the Long-Lived Asset Impairment Decision Male Financial Statement Preparers Only ($n = 78$).

Effect	Df	Type III SS	Mean Square	F-value	Prob > F
Motivation to manage earnings	1	0.005	0.005	0.00	0.967
Ability to manage earnings	1	8.894	8.894	3.12	0.082
Motivation × ability	1	9.293	9.293	3.26	**0.075**
Error	74	230.615	230.615	–	–

motivation for female preparers at the 5% level of significance and for male preparers at the 10% level of significance. This confirms that preparers who had the ability and/or motivation to manage earnings made different impairment decisions than preparers in the control group and that both female and male financial statement preparers were managing earnings.

What is not apparent from the ANOVA results is how the earnings management activities of female preparers differed from those of their male counterparts. To shed light on this, we examined the means of the reporting

Table 6. Mean Long-Lived Asset Impairment Decisions by Gender and Experimental Group (1 = Definitely will Not Report Impairment Loss, 7 = Definitely will Report Impairment Loss).

Experimental Group	*n*	Impairment Decision Mean
Male preparers		
Control	21	3.381
Motivation to manage earnings	15	2.667
Ability to manage earnings	20	**2.000***
Moral hazard	22	2.682
Female preparers		
Control	9	1.889
Motivation to manage earnings	10	**4.000****
Ability to manage earnings	11	**3.545***
Moral hazard	11	2.727

Note: Statistical significance tested using the Tukey HSD test.
*Statistically significantly different than the control group mean at the 5% level.
**Statistically significantly different than the control group mean at the 10% level.

decisions by experiment group and gender, and we ran the Tukey Honestly Significant Difference (HSD) multiple comparison procedure to determine which means were statistically significantly different. The results are presented in Table 6.

A review of the means in Table 6 suggests that female financial statement preparers became more conservative in their impairment decisions when they had the ability and/or motivation to manage earnings. In other words, they were more likely to report an impairment loss when they had private information and/or a profit-sharing plan than when they did not. Male preparers, however, became more aggressive in their impairment decisions when they had the ability to do so. The males in our study were less likely to report an impairment loss when they possessed private information.

Overall, these results suggest that, in the presence of an important relationship, female financial statement preparers respond differently to moral hazard conditions than their male counterparts. Therefore, H1 is supported.

H2 focuses solely on the impact on impairment decisions of the ability to manage earnings. This hypothesis suggests that, due to relationship concerns, private information alone may affect the decisions of female preparers in a different manner than the decisions of male preparers. Once again examining means in Table 6, it is apparent that possessing private information makes females more conservative and males more aggressive in their

reporting decisions. Thus, even without a motivation to manage earnings, females were more likely and males were less likely to report an impairment loss when they had private information than when they did not. This provides support for H2 (Table 6).

H3 focuses solely on the impact on impairment decisions of the motivation to manage earnings. In other words, is motivation alone sufficient to cause preparers to manage earnings? Examining the means in Table 6 indicates that male preparers with a motivation to manage earnings (but without an ability to manage earnings) did not make significantly different decisions than males without that motivation. However, female preparers with a profit-sharing plan made more conservative impairment decisions than females who did not have a profit-sharing plan. This provides some support for H3.

DISCUSSION AND CONCLUSIONS

The financial statement preparers participating in this study made a long-lived asset impairment decision in the presence of important relationship issues. The relevant accounting standard guiding the reporting decision provided opportunities for preparers to manage earnings through the exercise of professional judgment.

The results indicate that female financial statement preparers responded differently than their male counterparts to the case facts, when presented with an important relationship and moral hazard conditions in making long-lived asset impairment decisions. Females became more conservative in their long-lived asset impairment decisions when faced with moral hazard conditions. In contrast, males made more aggressive long-lived asset impairment decisions when they faced moral hazard conditions than when they did not. The female financial statement preparers in this study exhibited behavior that is inconsistent with agency theory, but supportive of ethics of care theory. Although a moral hazard condition existed, the females appear to have responded to the relationship present in the case facts as they became more conservative in their reporting decisions, even though this would lower reported earnings and the CFO's compensation. This finding is inconsistent with agency theory predictions.

Agency theory accurately described the behavior of male financial statement preparers in this study. They were less likely to report long-lived asset impairments when moral hazard conditions were present, which would increase reported earnings and the CFO's compensation.

As noted above, we cannot rule out gender-related differences in moral development or risk preferences as possible explanations for the behavioral differences we observed. However, we believe that differences in moral orientation provide a stronger explanation given the emphasis on personal relationship in our case setting. Reiter (1997) states, "If and when management is interested in preserving long-term relationships, their stories about corporate performance should be true" (p. 315). If one assumes that the more conservative corporate performance story, as told by the female preparers in our study, is more representative of truth, our findings are consistent with Reiter's assertion.

Given our results, we believe moral orientation (ethics of care v. ethic of rights) merits further study as a competing explanation for gender-related differences in behavior. Future studies could enhance this understanding by helping differentiate between the effects of moral orientation, moral development, and risk preferences on behavior.

Our results make sense in light of theoretical predictions that females have an affinity toward an ethic of care. As was expected from prior research, gender appears to be serving as a proxy for the likelihood of the financial statement preparers in the study to be concerned with the effect the decision outcome will have on relationships rather than on the effect for an autonomous decision maker. By providing evidence that an agent's ethical grounding can moderate the impact of moral hazard conditions, our results support Bohren's (1998) and Noreen's (1988) contentions that current principal–agent models need revision.

Our findings also support the link between the moral intensity model and decision-making behavior of financial statement preparers. Despite the presence of economic incentives, the female financial statement preparers in our study chose to forgo managing earnings. Our explanation, consistent with the ethics of care literature, is that female financial statement preparers were more sensitive to the relationship impacts such as proximity and concentration of effect, and thus more aware of the ethical dimensions of the reporting decisions they faced. The male financial statement preparers may have been less aware of the relationship or other ethical considerations, and thus were more susceptible to the moral hazard conditions as they appear to have made their reporting decisions using an economic maximization decision framework.

Although this study does not permit ruling out explanations of moral development and risk preference, taken as a whole the study provides empirical evidence that an accountant's worldview, including ethical outlook, may moderate self-interested behavior. This may cause him or her to act in

ways predicted by ethics of care as well as ways predicted by agency theory. Moreover, this study provides evidence of observable differences in behavior between men and women that can be attributed to concern for relationships, which is the underpinning for ethics of care literature. The study's empirical evidence cannot be directly and absolutely linked to an ethics of care perspective as it relates to adult behavior in a business or professional setting. However, these results suggest that ethics of care, an understudied theory, may be important to gender-related differences in decisions processes and should be the object of further study.

NOTES

1. SFAS No. 121 was superseded by SFAS No. 144 after the data collection for this study was completed. SFAS No. 121 allowed either a best-estimate approach or a probability-weighted approach to be used in developing forecasts of future cash flows. In the Exposure Draft for SFAS No. 144, the FASB proposed requiring the probability-weighted approach. However, after public input, the FASB decided to retain the two alternatives allowed under SFAS No. 121. The case used in this experiment is designed to allow either approach to be used. Furthermore, the asset is not impaired if the best-estimate approach is used. Under the probability-weighted approach, the asset is impaired. Therefore, the participants in the experiment could justify either reporting decision (the asset is impaired or not impaired), making it possible for the participants to manage earnings by their choice of method.
2. Participants in the moral hazard treatment group were exposed to both the motivation and ability treatments.
3. See, for example, Bernardi (1995), Bernardi and Arnold (1997), Clarke, Hill, and Stevens (1996), Cohen, Pant, and Sharp (1998), Eynon, Hill, and Stevens (1997), Etherington and Hill (1998), Etherington and Schulting (1995), Hill, Stevens, and Clarke (1998), Jones and Hiltebeitel (1995), Lampe and Finn (1992), Shaub (1994), Sweeney and Roberts (1997) and Sweeney (1995).
4. See Powell and Ansic (1997), for a review of this literature.

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DATA CONTAMINATION BY SOCIAL DESIRABILITY RESPONSE BIAS: AN INTERNATIONAL STUDY OF STUDENTS' CHEATING BEHAVIOR

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ABSTRACT

Our study examines the effect of social desirability on modeling cheating behavior using self-reported data. We believe that social desirability response bias contaminates many of the variables that previous research uses in modeling academic cheating. We initially examine the effect of variables in prior research to demonstrate that our sample is equivalent to those in prior studies. We then examine the effect of social desirability response bias on students' intolerance toward cheating; their cynicism about cheating; and one's intention to cheat in the future. We find that social desirability response bias contaminates students' self-reported data on cheating and the variables frequently used to predict cheating.

The evening news often contains stories feigning shock at corporate misconduct or criticizing our judicial system for not taking an aggressive stance

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on crime. Possible reasons for this behavior include the individual's upbringing or success-related pressures. Few suggest examining the individual's education even though cheating in college associates with unethical behavior in the workplace (Lawson, 2004; Sims, 1993). Lord and Melvin (1997, p. 15) believes that it is "our word against theirs" when it comes to being caught cheating and suggest that

> Given the recent litigation and administrative timidity, students and faculty may appear to be more tuned in to what they perceive to be the academic reality.

While numerous studies examine cheating among college students using self-reported data (Payne & Nantz, 1994); only one out of 96 business ethics articles using self-reported data considers social desirability response bias (SDRB) (Randall & Gibson, 1990). Because individuals usually respond in a socially desirable manner, Nyaw and Ng (1994) suggest that the validity of the findings of survey-based ethics studies that do not control for SDRB is subject to challenge.

In a study of business students from the Denmark, New Zealand, and the United States, Lysonski and Gaidis (1991, p. 148) conclude that "schools may be inadvertently overemphasizing technical training and ignoring ethical considerations." The gravity of the potential long-term effects of cheating is even more disturbing if one considers the growth in cheating over a 10-year period from 42 percent (Michaels & Miethe, 1989) to 80 percent (McCabe, 1999). A crucial point here is that neither of these studies considers SDRB; consequently, their results understate the actual level of cheating.

Bernardi and LaCross (2004) conducted a study controlling for SDRB using a sample of college business majors. These authors find that SDRB not only contaminates the dependent variable (whether or not a student had cheated) but also the independent variables that prior researchers commonly use such as cynicism, intolerance of cheating, intent to cheat, environment, punishment, and gender. This study expands upon the findings of Salter et al. and Bernardi and LaCross by controlling for SDRB using a culturally (Hofstede, 1980) diverse, international sample.

LITERATURE REVIEW

Overview

In our literature review, we select 20 studies (Table 1) published since 1990 that examine cheating in college that use the cynicism, intolerance, intent to

Table 1. Studies Examined in the Literature Review.

Author(s)	Year	(*n*)	SDRB	Int'l	Envir	Cyn	Intent	Punish	Intol	Gender
Bernardi and LaCross	2004	174	X		X	X	X	X	X	X
Ameen et al.	1996	320			X	X	X	X	X	X
Salter et al.	2001	370		X	X	X	X	X	X	X
Smith et al.	2002	606			X	X		X		X
Lord and Melvin	1997	97	3rd			X		X	X	
Smyth and Davis	2003	265				X		X	X	X
Tibbetts	1999	598	L				X			X
Tibbetts and Myers	1999	330					X	X		X
Haswell et al.	1999	562		X				X	X	X
Diekhoff et al.	1999	668		X				X	X	X
Davis et al.	1992	6,000						X	X	X
Payne and Nantz	1994	[22]						X		
Underwood and Szabo	2003	291		X					X	X
Allmon et al.	2000	227							X	X
Jensen et al.	2001	490							X	X
Borkowski and Ugras	1998	[56]								X
Cochran et al.	1998	448								X
Covey et al.	2001	110								X
Mitchell	2001	130								X
Lawson	2004	130								X

X, indicates that study examined variable.
L, acknowledges self-reported data as a limitation.
3rd, discussed the use of third-person wording as a means of controlling for SDRB.
Bracked data, Mega analyses (see Note 1).
Highlighted data, Accounting studies.
Int'l, International sample.

cheat, environment, punishment, and gender variables.[1] Three studies examine all of these variables, Ameen, Guffey, and McMillan (1996), Salter, Guffey, and McMillan (2001), and Bernardi and LaCross, which will be referred to as the "ASB studies" in this review. Five of the studies (25 percent) in our literature review examine the cheating behavior of accounting majors (highlighted data in Table 1) with results consistent with the other studies outside of accounting and business. Consequently, we use the studies outside of accounting to provide depth to our literature review and show that cheating and the attitudes that associate with cheating do not appear to vary by major.

Throughout this portion of the research, we will demonstrate that the literature concerning attitudes and behavior of accounting majors do not differ from the literature outside of accounting or even business. For

example, Randall and Gibson (1990) note in a critical assessment of ethics research that, while most ethics studies rely on self-reported data, only about 10 percent (90 percent) control (do not control) for SDRB. Consistent with Randall and Gibson, the Table 1 data indicate that only one study out of the 20 studies (five percent) controls for SDRB using a test instrument for this purpose. Other research either implicitly or explicitly (Lord and Melvin) assume that the use of third-person wording overcomes the problems that associate with SDRB. Lord and Melvin (1997, p. 5) provide an example of this assumption about controlling for SDRB in cheating research by wording the questions in the third person because

> All of the items are worded without reference to a respondent and, therefore, attitudes are inferred based upon a respondent's judgments of the behavior of others.

Geiger and O'Connell (2000) examine the control that by third-person wording provides by also controlling for SDRB using Paulhus' (1991) complete balanced inventory of desirable responding. Even though the wording of questions in their survey is in the third person, these authors find that SDRB is still a significant factor in all three of their dilemmas. SDRB explains between 3.4 and 17.2 percent of the variation (adjusted R^2) in the participants' responses leading Geiger and O'Connell (2000, p. 118) to conclude that

> [Using] a surrogate measure of social desirability response bias is less desirable than using a direct measure of this bias such as Paulhus' (1991, pp. 40–41) impression-management subscale scores.

Student Behavior

Our examination shows that, except for Bernardi and LaCross, no recent studies that examine academic dishonesty control for SDRB either nationally or internationally; however, only one of the 20 studies in Table 1 lists SDRB as a potential limitation to the research findings (Tibbetts, 1999). While acknowledging that SDRB is a problem with survey-based research on cheating, Lord and Melvin (Haswell, Jubb, & Wearing, 1999; Smith, Davy, Rosenberg, & Haight, 2002) believe that this type of bias should not be a problem if the questions refer to the behavior of others (promise students anonymity and confidentiality); however, they offer no empirical proof of this premise. Following the line of research Ameen et al. and Salter et al. establish, Bernardi and LaCross find that SDRB is significant in students' self-reported cheating behavior in a sample of students from the United States. These authors list the source of their sample (i.e., only one

country) as a research limitation that affects the generalizability of their research. Following this line of research, we examine an international sample of four countries. If Bernardi and LaCross' findings are robust, one would anticipate similar findings for an international sample and our first hypothesis is (the wording of all hypotheses is in the alternate form)

H1. As social desirability response bias increases, self-reported CHEATING behavior will decrease.

Student-Attitudes and Social Desirability Response Bias

Five recent studies regarding cheating in college report that cynicism associates with cheating behavior. Cynicism is the general distrust of the integrity or professed motives of others. Ameen et al. as well as Salter et al. measure cynical attitudes by the extent of participants' agreement with three statements taken from Sierles, Hendrickx, and Circle (1980) such as "everybody steals, cheats, or lies at least once in his/her lifetime." Results show cheaters are significantly more cynical than those who did not report having cheated. Additionally, Smith et al. and Lord and Melvin note that justifying (i.e., a form of cynicism) one's behavior associates with self-reported cheating.

Ameen et al. (1996, p. 197) indicate that "cynical individuals are more inclined to engage in academic dishonesty"; Salter et al. reports similar results. Bernardi and LaCross also examine cynicism, but they control for the effect of SDRB. Their results show that, as socially desirable responding increases, the respondents' cynical attitudes about cheating decreases. For example, the ASB studies all use the following questions to measure cynicism:

1. People who say they have never cheated before are hypocrites.
2. Everybody steals, cheats, or lies at least once in his/her lifetime.
3. People have to cheat in this "dog-eat-dog" world.

If one was interviewing a student or prospective employee, and their responses include any of the above thought patterns, one would likely conclude that they had cheated in the past (i.e., responses 1 and 2) and probably would do so in the future (i.e., response 3). Consequently, we propose that cynicism is a socially undesirable trait as well as stating that cynics are more likely to engage in academic dishonesty. This data suggest a further examination of the results of Ameen et al. and Salter et al. results controlling for SDRB.

H2. As social desirability response bias increases, self-reported CYNICISM decreases.

Lord and Melvin note that students are relatively tolerant of cheating; however, they did not find an association between being tolerant and actually cheating. The ASB studies, among others, also examine students' intolerance toward cheating and whether or not they believe that it is a problem. The ASB studies all report that intolerance has the highest association with a student's self-reported cheating behavior. Salter et al. (2001, p. 46) state that

> The more often students perceive questionable actions as being a severe form of cheating the less likely they are to cheat themselves.

However, according to research, many students do not view these "questionable actions" as severe. Smyth and Davis (2003, p. 5) reports that although

> Nearly all respondents believe that cheating is ethically wrong (92 percent), a surprising 45 percent find cheating to be socially acceptable.

Findings by Davis, Grover, Becker, and McGregor (1992), Haswell et al. (1999), and Jensen et al. (2001) support the notion that students' academic integrity is alarmingly low, leading to the conclusion that they will be more apt to cheat in the future. This increases the potential impact of Ameen et al.'s (1996) conclusion that "better monitoring and enforcement could possibly reduce the propensity to cheat." However, open-ended questions are the basis for this conclusion and the survey data could associate with SDRB. Bernardi and LaCross report that, as socially desirable responding increases, one's intolerance for cheating increases. For example, students desiring to be seen as "good and honest" would report being more intolerant of cheating than those who respond honestly.

H3. As social desirability response bias increases, self-reported INTOLERANCE toward cheating will increase.

Few studies examine one's intention to cheat in the future. Tibbetts and Myers (1999, p. 192) suggest that "higher perceptions of anticipated pleasure of cheating and friends' cheating behavior led to more cheating intent by the respondent." ASB are among the few studies that control for intent, each finding that students who intend to cheat in the future have a higher incidence of self-reported cheating. Again, Bernardi and LaCross indicate that SDRB contaminates students' self-reported intention to cheat in the future. The lower the SDRB score (i.e., participant responds more honestly), the higher their intent to cheat in the future. Consequently, those participants with a high SDRB score claim they have little intention of cheating in the future.

H4. As socially desirable responding increases, the self-reported INTENTIONS to cheat in the future will decrease.

Student Perceptions and Social Desirability Response Bias

Smith et al. suggest that vigilant supervision can reduce the level of cheating on examinations. The ASB studies also examine the academic environment and how it affects whether or not a student will cheat. Ameen et al. ask students to indicate whether or not they have ever seen a classmate cheat. Ameen et al., Salter et al., and Smith et al. find that seeing a classmate cheat without getting caught leads other students to believe that they can also cheat. Haswell et al. (1999, p. 234) conclude that "increased risk of detection is not effective unless followed up by a strong penalty," which supports Smith et al. finding. Bernardi and LaCross examine the environment and find similar results in that the academic environment influences whether or not a student will cheat. However, they find no evidence of contamination due to SDRB; consequently, we believe that a similar association will exist in an international sample

H5. An association will not exist between socially desirable responding and students' perceptions of the level of cheating in the surrounding academic ENVIRONMENT.

Some believe that students who perceive a high likelihood of being caught are less likely to cheat. The ASB and Smith et al. studies also examine fear of punishment; each finds a negative relationship between punishment and the propensity to cheat. However, Ameen et al. (1996, p. 202) suggest that "students felt most professors do not want the aggravation of enforcing rules against cheating." Additionally, Smyth and Davis (2003, p. 5) note that "observing others being caught cheating has little influence on the fear of being punished," which coincides with the student attitudes in Payne and Nantz (1994). Lord and Melvin report that faculty hold harsher attitudes about the appropriate punishment for cheating than students. In fact, Haswell et al. indicate that the willingness to participate in cheating dramatically declined as the penalty increased. Salter et al. and Ameen et al. note that, while punishment is significant factor determining the cheating behavior of students from the US, punishment is not deterrent for students from the UK.

In a cross-national study, Diekhoff, LaBeff, Shinohara, and Yasukawa (1999) compare the responses of American students and Japanese students about the importance of particular deterrents to cheating. Among those who admit to cheating, the biggest deterrent to cheating is the fear of punishment for both American and Japanese students. However, for those who did not

report having cheated, guilt is the most significant deterrent. While Diekhoff et al. do not find any association with culture, they report a difference in the mindset between cheaters and those who do not cheat. Bernardi and LaCross find no evidence of contamination when they control for SDRB.

H6. No association exists between socially desirable responding and students' perceptions of the level of PUNISHMENT resulting for cheating.

Gender

Gender is the variable most commonly controlled for in cheating research in the current studies. Smith et al. find that female accounting majors are less likely to report having cheated than their male counterparts. Davis et al. (1992), Ameen et al., Cochran, Wood, Sellers, Wilkerson, and Chamlin (1998), Allmon, Page, and Roberts (2000), Salter et al., and Smyth and Davis (2003) also report significant results indicating that male students are more likely to cheat than their female counterparts. Borkowski and Ugras (1998) analyze 56 past studies and the variables that each consider. Their results suggest that 23 of those controlled for gender and that male students are more likely to cheat than female students. However, Tibbetts and Myers (1999), Covey, Saladin, and Killen (2001), Mitchell (2001), and Lord and Melvin find no significant gender effect; indeed, Diekhoff et al. (1999, p. 348) indicate that their research

> suggests that the effect of gender on cheating is weak, at best, and the difference in the gender distributions of our samples is probably relatively unimportant.

Underwood and Szabo (2003) report significant gender effects; however, the effect is not as straightforward as many studies indicate. These authors find that "both males and females may commit offences but the stimulus for such behavior may differ" (p. 475). Their results suggest that, while male students are more likely to cheat, the situation behind cheating is more relevant than most studies acknowledge. For example, Lawson (2004) find that female students believe more strongly that it is OK to lie on an employment application and use a fake ID to purchase alcohol (i.e., forms of cheating). Smith et al. find that female accounting majors tend to neutralize (i.e., justify) more in order to reduce the guilt of cheating. Using international samples, Whipple and Swords (1992), Lysonski and Gaidis (1991) and Haswell et al. (1999) find that female students from Australia, Denmark, New Zealand, South Africa, the UK, and the US demonstrate higher business ethics (i.e., countries similar to the current research).

Bernardi and LaCross indicate that SDRB contaminates the responses from both the male and female students. For the groups with low SDRB scores (meaning more honest), both male and female students report a higher level of cheating. On the other hand, both male and female students who score higher on the SDRB scale report lower levels of cheating. The high SDRB score indicates that participants alter their responses to give the impression that they are ''ethically correct and honest,'' which suggests contamination by SDRB. To be consistent with prior research, we control for gender in this research. Bernardi, Delorey, LaCross, and Waite (2003) report that, after controlling for SDRB, the attitudes by gender only differ for one of five unethical dilemmas; male students perceive this scenario as being more unethical.

Summary of the Literature

The key point in our literature review is that prior research fails to control for SDRB; consequently, the results of prior research are subject to question. This research examines the area of students' self-reported cheating behavior (i.e., a socially undesirable behavior). As most individuals learn to act in a socially desirable manner, it is unreasonable for researchers to assume that they will respond in a totally honest manner to questions about their behavior in extremely sensitive areas even when told they have anonymity. Consequently, we believe that SDRB contaminates most of the variables this research stream considers.

SUBJECTS AND MEASURES

Participants

Our sample includes the responses of 290 college business students from Australia (54), China (88), Ireland (101), and Japan (47). For comparison purposes, we also include the data from the 174 business majors from the United States (Bernardi & LaCross, 2004).

Survey Procedures

Our research instrument includes Salter et al.'s questionnaire on cheating (Appendix A), the measure of SDRB (Appendix B), and a brief background questionnaire. The authors made inquiries to determine whether our research instrument should be in the country's language. As our sample from China

comes from a university where classes are in English, only the questionnaires for Japan had to be translated. For Japan, one person first translated the survey questionnaire into Japanese and a second person translated the questionnaire back into English to ensure that the initial translation was correct. Both of the individuals who translated the questionnaire data are exchange students from Japan studying at our university. Our exchange students indicate that the questionnaire is clear and that it should not present any problems.

One of the background questions requests the participant's home country; we include this question so that we could identify students who are not from the sampled country. For example, two of the students in the initial sample from Australia are study abroad students from other countries and are not in the final sample. The surveys were delivered to professors in a country by study abroad students from our university and completed during class time.[2] The faulty members assisting us with the survey told the participating students that the researchers requesting the information would only receive an Excel file containing the survey data. Additionally, the survey has no area for a student's name.

Dependent Variables

We use the same variables in this research that Bernardi and LaCross, Salter et al., Ameen et al., and Sierles et al. use (Table 2). CHEAT1 is the sum of four self-reported cheating behaviors: (1) on a major test, (2) on a minor

Table 2. Variables and Hypothesized Relationship to Cheating.

Variable	Association with Cheating	Data for Four Countries in Sample				B & L (2004) US
		Australia	China	Ireland	Japan	
CHEAT1	NA	1.43	1.34	0.88	1.83	1.18
CHEAT2	NA	0.57	0.71	0.51	0.72	0.62
CYNICISM	Positive	3.13	2.32	2.53	3.04	2.71
ENVIRONMENT	Positive	0.96	0.88	0.57	0.68	0.92
GENDER	Positive	52/48	30/70	40/60	64/36	58/42
SDRB	Negative	5.44	5.67	5.72	7.32	5.09
INTENT	Positive	0.42	0.49	0.26	0.43	0.43
PUNISHMENT	Negative	0.50	0.41	0.73	0.81	0.51
INTOLERANCE	Negative	2.69	2.59	3.04	3.28	3.08
(*N*)	NA	54	88	101	47	174

B & L, Bernardi and LaCross.
Gender, MM/FF represents the percentage of male/female students in the sample.

test, (3) on a major project, and (4) on a minor project (Appendix A: Personal experience questions 5 through 8). CHEAT1 has a range of zero (i.e., someone who did not report cheating on any of the four behaviors) to four (i.e., someone who reported cheating on all of the four behaviors). CHEAT2 is a dichotomous variable coded as one if the participant reports cheating on any one or a combination of the four cheating behaviors in CHEAT1, or zero if the participant did not report cheating.

Student Attitude and Perception Variables

The five independent student variables we use form two groups – student attitudes and perceptions. The student attitudes group refers to how a student views the act of cheating on a personal level and includes the level of cynicism a student has toward cheating, their personal level of intolerance toward cheating, and their intention to cheat in the future. The student perceptions of how an instructor will punish them and the environment (whether or not fellow classmates cheat) also affect whether or not they cheat.

The students' attitude variables are cynicism, intolerance, and intent. CYNICISM is the average of each student's responses for the three questions on CYNICISM, which have a range of zero to five (Appendix A: Cynicism questions). INTOLERANCE is the average of each student's responses to the 23 questionable academic practices (Appendix A: Questionable academic practices questions). Higher averages indicate a higher INTOLERANCE for cheating (range of zero to five). INTENT is an indicator variable about whether students expect to cheat (one) or not cheat (zero) in the future (Appendix A: Personal experience question 9).

The student perceptions variables are PUNISHMENT and ENVIRONMENT. PUNISHMENT relates to questions dealing with getting caught cheating and is set at one (zero) for the two most (three least) severe penalties (Appendix A: Personal experience question 12). ENVIRONMENT is an indicator variable, which is one (zero) if student has (has not) witnessed another student cheating on an exam (Appendix A: Personal experience question 1). If students continually see other students cheat and are not caught, this perception could lead them to cheat. Gender is an indicator variable set to one for men and zero for women.

Social Desirability Response Bias

As this research specifically examines the potential contamination of prior models by SDRB on an international sample, Paulhus' impression

management subscale (IMS) is part of the research instrument (Appendix B). While there are several instruments available to measure SDRB, we use the IMS subscale of Paulhus' (1991) balanced inventory of desirable responding (BIDR) to measure SDRB in this study for three reasons. First, Randall and Fernandes (1991) indicate that the IMS has the highest overall correlation among four different measures of socially desirable responding. Second, the IMS is the most recent of these four measures (1986 versus 1960 to 1975). Finally, the IMS provides an overall scale that is 13 items shorter than the Marlow-Crowne scale (Crowne & Marlowe, 1960) with similar internal consistency (0.75– 0.86 for Paulhus' IMS versus 0.73–0.88 for the Marlowe-Crowne scale).

The IMS portion of the balanced inventory of desirable responding (BIDR) is a 20-item subscale. Every other statement is reverse coded (e.g., odd/even numbered statements are similarly coded). One scores the odd (even) numbered responses as one if the participant answers is either one or two (six or seven) – other responses are coded as zero. The overall score on the IMS is the total of the points (one or zero for each statement) on the 20 questions. Consequently, scores range from zero (20) indicating the participant does not respond (responds) in a (in an extremely) socially desirable manner; higher scores indicate the magnitude of socially desirable responding.

Paulhus (1991) indicates that the full BIDR (IMS) has a concurrent validity of 0.71 with the Marlowe-Crowne scale. The IMS has an internal consistency coefficient of 0.79–0.86 (Paulhus, 1991); in a separate study, Randall and Fernandes report an internal consistency of 0.79. Individuals exhibiting SDRB cause the test score on each of these tests to increase indicating a higher propensity to respond in a socially desirable manner.

DATA ANALYSIS

Models for Cheating

Table 3 shows the models for both CHEAT1 (Panel A) and CHEAT2 (Panel B) for the samples from Australia, China, Ireland, and Japan. In the modeling process, we use indicator variables for the countries with Ireland as the null variable. The model for CHEAT1, which only Bernardi and LaCross use, explains 43.1 percent of the variation (adjusted R^2) in student behavior. The most significant variable is a student's INTENT to cheat in the future ($p = 0.0001$); those who intend to cheat in the future have a higher rate of self-reported cheating. The model also indicates that students who are more CYNICAL about others' cheating behavior are more likely to report having

Table 3. Regression Models for Cheating Behavior.

Panel A: Model for CHEAT1 (sum) without US

Model	Adj R^2	F Fact	Signif	N
Regress	0.431	30.86	0.0001	290

Term	Coeff	T Stat	P-value	Part AdjR^2
Intercept	1.54	7.29	0.0001	
Intent	0.35	5.21	0.0001	0.241
Cynicism	0.19	3.87	0.0001	0.067
SDRB	−0.09	−4.72	0.0001	0.044
Japan	0.37	4.46	0.0001	0.040
Environ	0.26	3.76	0.0002	0.029
Punish	−0.14	−2.24	0.0259	0.010

Panel C: Model for CHEAT1 (sum) with US

Model	Adj R^2	F Fact	Signif	N
Regress	0.383	46.33	0.0001	464

Term	Coeff	T Stat	P-value	Part AdjR^2
Intercept	1.98	9.59	0.0001	
Intent	0.40	7.34	0.0001	0.248
SDRB	−0.08	−4.15	0.0001	0.040
Japan	0.43	5.49	0.0001	0.040
Environ	0.29	4.61	0.0001	0.027
Cynicism	0.14	3.59	0.0004	0.013
Intolerance	−0.17	−3.35	0.0009	0.015

Panel B: Model for CHEAT2 (Yes/No) without US

Model	R^2	χ^2	Prob > χ^2	N
Regress	0.268	221.47	0.1340	290

Term	Coeff	χ^2	Prob > χ^2	Part R^2
Intercept	−2.37	33.67	0.0001	
Intent	−0.77	19.44	0.0001	0.150
SDRB	0.21	19.14	0.0001	0.046
Environ	−0.56	11.22	0.0008	0.029
Japan	−0.71	10.04	0.0015	0.022
Punish	0.43	7.50	0.0062	0.021

Panel D: Model for CHEAT2 (Yes/No) with US

Model	R^2	χ^2	Prob > χ^2	N
Regress	0.288	339.33	0.0001	464

Term	Coeff	χ^2	Prob > χ^2	Part R^2
Intercept	−2.05	15.19	0.0001	
Intent	−0.72	25.21	0.0001	0.168
SDRB	0.14	11.54	0.0007	0.033
Environ	−0.63	16.28	0.0001	0.023
Japan	−0.72	10.28	0.0013	0.017
Cynicism	−0.31	9.11	0.0025	0.010
Intolerance	0.35	6.57	0.0104	0.013
Punish	0.28	5.05	0.0246	0.009

cheated ($p = 0.0001$). As Bernardi and LaCross report, SDRB inversely relates to self-reported cheating behavior ($p = 0.0001$). Students from Japan have a significantly higher rate of self-reported cheating. As the environment becomes less threatening (i.e., students witness other students cheating) cheating increases. However, students who perceive harsher consequences (e.g., PUNISHMENT) for cheating report a lower incidence of cheating.

CHEAT2 is an indicator variable that reflects whether a student cheated (one) or not cheated (zero) in the past on any of the four categories of cheating we survey. Because CHEAT2 is a dichotomous variable, we use logistic regression model. The model for CHEAT2 (Panel B) indicates that a student's INTENT to cheat in the future is also the most significant predictor of the prior cheating behavior. SDRB is the next most significant

variable ($p = 0.0001$) followed by ENVIRONMENT ($p = 0.0008$), JAPAN ($p = 0.0015$), and PUNISHMENT ($p = 0.0062$). We provide these analyses to demonstrate the similarity of our data with the data in prior research (Bernardi & LaCross and Salter et al.).

Table 3 also shows the models for both CHEAT1 (Panel C) and CHEAT2 (Panel D) for the samples from Australia, China, Ireland, Japan, and the United States (i.e., Bernardi and LaCross' sample). In this part of the modeling process, we use indicator variables for the international countries with the United States as the null variable. The data in Panels C and D demonstrate the consistency of the models even when adding a large sample from the United States ($n = 174$) to our international sample ($n = 290$).

The data indicate that, as the level of SDRB increases (i.e., students respond less honestly), the level of self-reported cheating decreases, which creates an inverse or negative association between the two variables. The results are nearly the same whether or not the United States is in the sample. Interestingly, our adjusted R^2 for SDRB mirrors that of Geiger and O'Connell. Our analysis of cheating behavior and SDRB (Table 3) highlights the impact of SDRB on self-reported academic dishonesty. The self-reported academic dishonesty of the students from Australia, China, Ireland, Japan, and the United States significantly associates with their propensity to respond in a socially desirable manner. The low SDRB group (i.e., the more honest respondents) reports a higher amount of cheating behavior; the reverse is true for the high SDRB group that self-reported a lower level of cheating behavior. This indicates a significant degree of contamination of the variables many use to measure academic dishonesty by SDRB. Consequently, our results demonstrate the need to control for socially desirable responding in self-reported cheating research.

Cheating and Social Desirability Response Bias

We also examine our data for CHEAT1 and CHEAT2 and SDRB, which has range a from zero (i.e., responds to survey questions honestly) to 20 (i.e., responds to survey questions in a highly socially desirable manner), using a median-split procedure. The ranges of scores at the bottom of Table 4 reflect the results of the median split by country. For example, while the low range for the United States and Australia is zero to four, the low range for China and Ireland (Japan) is zero to five (two to six).

In our analysis, we classify those students at or below (above) the median as zero (one). If cheating behavior does not associate with socially desirable responding, the level of self-reported cheating (CHEAT1 or CHEAT2)

Table 4. Cheating Behavior by Response Bias.

Range of SDRB	Australia	China	Ireland	Japan	US
Panel A: Cheating as a percentage of total (CHEAT1)					
Low SDRB	51.1	39.4	32.7	68.0	36.3
High SDRB	29.2	27.3	9.2	20.5	23.3
Difference	21.9	12.1	23.5	47.5	13.0
Significance	0.0305	0.0502	0.0001	0.0001	0.0043
Panel B: Cheating as a percentage of students (CHEAT2)					
Low SDRB	66.7	73.3	72.7	88.0	72.6
High SDRB	50.0	67.4	23.9	54.5	52.2
Difference	16.7	5.9	48.8	33.5	20.4
Significance	0.2211	0.5453	0.0001	0.0158	0.0061
Low SDRB	0–4	0–5	0–5	2–6	0–4
High SDRB	Above 4	Above 5	Above 5	Above 6	Above 4

should not differ between the two levels of SDRB. CHEAT1 is the percentage of the total possible cheating behaviors; as CHEAT1 has a range of zero to four, the interval between each level was 25 percent. For example, if a participant did not report cheating on any of the four possible situations, CHEAT1 would be zero. Similarly, an individual cheating on three (all four) of the four items would have a score of 75 (100) percent.

Panel A of Table 4 shows that the self-reported cheating behavior, which CHEAT1 measures, of the low SDRB group (i.e., those who respond more honestly) is higher for all five countries than the self-reported cheating of the high SDRB group (i.e., those who respond less honestly). Using a univariate analysis, the difference is significant for the samples of all countries at the 0.05 level except for Australia, which is significant at the 0.10 level. We also test our model using a zero-one approach to cheating (i.e., referred to as CHEAT2). We classify those students who report (not) cheating on one or more (any) of the events as one (zero). However, for CHEAT2, the difference between the two groups is only significant at the 0.05 level for the samples from Ireland, Japan, and the United States.

Our key finding here is that self-reported cheating significantly associates with SDRB. This finding verifies the concern prior researchers only express in the limitations section. The data indicate that the highest (lowest) rate of self-reported cheating actually occurs for the group with the lowest (highest) SDRB scores. Consequently, the data suggest that SDRB contaminates the dependent variable (i.e., self-reported cheating behavior) in prior studies.

Student Attitudes and Social Desirability Response Bias

We examine the student attitude variables and their association with socially desirable responding using the median-split procedure. CYNICISM is the average of each student's response for the three questions on CYNICISM, which has a range of zero to five. The data in Panel A of Table 5 indicate that CYNICISM is lower for the high SDRB group for Australia, Ireland, Japan and the United States. The higher group reports being less cynical about others' behavior (highlighting indicates the difference is opposite to what we anticipated). Using a univariate analysis, these differences are significant at the 0.05 level for Australia, Ireland, and the United States and approaches significance for Japan.

INTOLERANCE is the average of each student's responses to the 23 questionable academic practices. Higher averages indicate a higher intolerance for cheating (range from zero to five). Panel B of Table 5 provides the comparisons for INTOLERANCE of cheating. In all cases, the data indicate that students who respond in a more socially desirable manner report a higher

Table 5. Cynicism about Cheating and Intention to Cheat by Response Bias.

Range of SDRB	Australia	China	Ireland	Japan	US
Panel A: Cynicism about cheating					
Low SDRB	3.57	2.18	2.84	3.29	2.90
High SDRB	2.73	2.47	2.15	2.74	2.53
Difference	0.84	−0.29	0.69	0.55	0.37
Significance	0.0280	0.3111	0.0020	0.1434	0.0516
Panel B: Intolerance of cheating					
Low SDRB	2.56	2.20	2.73	2.96	2.89
High SDRB	2.79	3.00	3.41	3.63	3.26
Difference	−0.23	−0.80	−0.68	−0.67	−0.37
Significance	0.3595	0.0089	0.0001	0.0143	0.0028
Panel C: Intention to cheat					
Low SDRB	65.2	60.0	35.8	64.0	57.1
High SDRB	23.3	37.2	15.2	18.2	29.5
Difference	41.9	22.8	20.6	45.8	27.6
Significance	0.0031	0.0341	0.0233	0.0027	0.0003
Low SDRB	0–4	0–5	0–5	2–6	0–4
High SDRB	Above 4	Above 5	Above 5	Above 6	Above 4

level of INTOLERANCE toward cheating. The univariate analyses indicate that, except for Australia, all of the differences are significant at the 0.01 level.

INTENT is an indicator variable about whether the student expected to cheat (one) or not cheat (zero) in the future. The data in Panel C of Table 5 report the average response rate for each group of students. The comparisons for INTENT to cheat in the future indicate that students who respond in a more socially desirable manner report a lower INTENT to cheat in the future for the samples from all five countries. For example, in Australia, 65.2 percent of the low SDRB report an intention to cheat in the future versus 23.3 of the high SDRB. The univariate analyses indicate that all of the differences are significant at the 0.05 level.

The contamination of the CYNICISM (INTOLERANCE) variable by SDRB is significant for the samples from all countries except China (Australia). The data indicate that, as socially desirable responding increases, self-reported CYNICISM (INTOLERANCE) about academic dishonesty decreases (increases). Those who respond in a socially desirable manner report that they did not believe that many of their fellow classmates cheat and that they personally are intolerant of academic dishonesty. A student's INTENTION to cheat in the future is the strongest indicator of academic dishonesty. Although many studies use this variable, none account for the biasing of student responses that associates with SDRB. Contamination by SDRB is highest for this variable; students are more likely to respond to questions about their intent based on what they "should say." Students scoring high on the SDRB index (i.e., less honest responding) report lower INTENTIONS to cheat in the future.

Student Perceptions and Social Desirability Response Bias

PUNISHMENT relates to questions dealing with getting caught cheating, which was set to zero for the three least severe penalties: (1) nothing more than a reprimand; (2) be forced to retake the exam; and, (3) have course grade lowered by a letter or more. PUNISHMENT is set to one for the two most severe penalties: (1) receive an F in the course and (2) be suspended from the university for at least one semester. Panel A of Table 6 shows that PUNISHMENT did not differ by SDRB group except for the students from Australia, which approaches significance ($p = 0.1035$).

ENVIRONMENT is an indicator variable set to one (zero) if student had (had not) witnessed another student cheating on an exam. If students continually see other students' cheat, but not get caught, this perception could lead them to cheat. While there is not a difference in the responses of the two

Table 6. Punishment and Environment by Response Bias.

Range of SDRB	Australia	China	Ireland	Japan	US
Panel A: Punishment as a percent					
Low SDRB	37.5	35.6	69.1	76.0	52.4
High SDRB	60.0	46.5	78.3	86.4	50.0
Difference	−22.5	−10.9	−9.2	−10.4	2.4
Significance	0.1035	0.2972	0.3017	0.3730	0.7536
Panel B: Environment as a percent					
Low SDRB	95.8	80.0	69.1	84.0	92.9
High SDRB	96.7	95.3	43.5	50.0	91.1
Difference	−0.9	−15.3	25.6	34.0	1.8
Significance	0.8723	0.0448	0.1050	0.0166	0.6728
Low SDRB	0–4	0–5	0–5	2–6	0–4
High SDRB	Above 4	Above 5	Above 5	Above 6	Above 4

groups for the students from Australia and the United States (Panel B of Table 6), there is a significant difference between the low SDRB and high SDRB groups for the Japanese students ($p = 0.0166$). The high SDRB group reports witnessing more cheating than the low SDRB group. The same relationship is true for the students from Ireland; however, the difference only approaches significance at the 0.10 level. Finally, the relationship reverses for the sample from China (highlighted data) with the high SDRB group witnessing more cheating ($p = 0.0448$).

The last two independent variables measure a student's reaction to the potential threat of PUNISHMENT and to witnessing other students cheating (ENVIRONMENT). Responses vary by SDRB for the samples from China (positively) and Japan (negatively) for the ENVIRONMENT variable; ENVIRONMENT does not associate with SDRB for the students from Australia, Ireland, and the United States. PUNISHMENT does not significantly associate with socially desirable responding. Finally, consistent with Bernardi et al. (2003), our results indicate that, after controlling for SDRB, there is not a difference in self-reported academic dishonesty between male and female students.

Testing the Robustness of Our Findings

We also analyze the data using different cutoffs. For example, while we use a cutoff of 4 (5) as the upper bound of the low SDRB group for Australia and

the US (China and Ireland) in our prior analysis in this paper, Table 7 shows the results of our testing using a cutoff 5 (4) as the upper bound of the low SDRB group for Australia and the US (China and Ireland). The results of this analysis are nearly identical to those in Tables 4 through 6. The only noticeable difference is in the area of punishment where the averages from

Table 7. Research Results using Different Bounds for SDRB Cutoffs.

Range of SDRB	Australia	China	Ireland	Japan	US
Panel A: Cheating as a percentage of total (CHEAT1)					
Low SDRB	43.8	39.3	32.5	76.5	35.5
High SDRB	30.4	30.0	15.2	28.3	21.6
Significance	0.2198	0.1317	0.0014	0.0001	0.0025
Panel B: Cheating as a Percentage of students (CHEAT2)					
Low SDRB	60.6	74.3	70.0	94.1	71.0
High SDRB	53.0	67.9	37.7	56.7	50.0
Significance	0.5518	0.5228	0.0019	0.0221	0.0052
Panel C: Cynicism about cheating					
Low SDRB	3.26	2.21	3.02	3.43	2.90
High SDRB	2.92	2.39	2.20	2.81	2.46
Significance	0.3525	0.5342	0.0004	0.1119	0.0194
Panel D: Intolerance of cheating					
Low SDRB	2.47	2.30	2.69	2.71	2.97
High SDRB	2.99	2.78	3.26	3.60	3.31
Significance	0.0022	0.1312	0.0015	0.0013	0.0019
Panel E: Intention to cheat					
Low SDRB	59.4	62.9	38.5	70.6	55.0
High SDRB	17.4	40.4	18.3	26.7	26.4
Significance	0.0026	0.0418	0.0262	0.0051	0.0002
Panel F: Punishment as a percent					
Low SDRB	42.4	40.0	77.5	76.5	52.4
High SDRB	60.5	41.5	70.5	83.3	50.0
Significance	0.1660	0.8879	0.4376	0.5672	0.7942
Panel G: Environment as a percent					
Low SDRB	93.9	80.0	72.5	94.1	94.0
High SDRB	99.6	92.5	47.5	53.3	89.2
Significance	0.9481	0.0856	0.0261	0.0158	0.2550
Low SDRB	0–5	0–4	0–4	2–5	0–5
High SDRB	Above 5	Above 4	Above 4	Above 5	Above 5

Ireland are now highlighted. The averages change from 69.1 and 78.3 for a cutoff for the low group of SDRB of 5 to 77.5 to 70.5 for a cutoff of 4.

CONCLUSIONS

Although a few studies list SDRB as a limitation to their findings, none of the research we examine suggests contamination by SDRB except Bernardi and LaCross, who extensively examine its overall effect on self-reported cheating. Our study expands the research of Bernardi and LaCross to an international sample; the results of this study mirror those of Bernardi and LaCross. Consequently, our examination of four countries provides confirming data indicating that SDRB contaminates not only the dependent variable (whether or not a student will report having cheated), but also the independent variables.

Our finding that socially desirable responding results in lower levels of self-reported cheating suggests that cheating is a greater problem than earlier studies acknowledge. Owing to the similarity in the findings of prior research and this research using different sets of majors in our literature review, we believe our results indicate a grave problem. Viewed from the prospective of the growing rate of cheating among college students, the data in this research imply that our thoughts on the appropriate punishments for being caught cheating appear to be ineffective. For example, if getting caught cheating results in failing the course and the student will fail if they are honest, then we suggest that this punishment is ineffective.

We believe that there has been sufficient research indicating a pandemic of cheating in our educational institutions. The teaching community must acknowledge that what we consider adequate deterrents to cheating have not been effective in reducing the incidence of cheating. Consequently, our research suggests that schools should consider adopting policies that follow their values of integrity and that those caught cheating on examinations should be dismissed from the institution. If this were the case, the act of cheating has actual economic consequences. For example, at private schools, the consequence would be approximately $10,000 (i.e., a low estimate) in lost tuition and having their transcript reflect their inappropriate behavior. This suggestion leads to an interesting line of research that studies the effectiveness of enforcing codes of conduct with meaningful punishments for academic dishonesty.

Our research has three apparent limitations. The first limitation is that we use Paulhus' measure of SDRB; future research should use other measures

Power Distance (1980: 106)

01 – 10	11 – 20	21 – 30	31 – 40	41 – 50	51 – 60	61 – 70	71 – 80	81 – 90	91 – 100
	DN (18)	IR (28)	US (40) AU (36) **SW (31)**		JA (54)			**VN (81)**	**PH (94)**

Uncertainty Avoidance (1980: 165)

01 – 10	11 – 20	21 – 30	31 – 40	41 – 50	51 – 60	61 – 70	71 – 80	81 – 90	91 – 100
		SW (29) **DN (23)**	IR (35)	**PH (44)** US (46)	AU (51)		**VN (76)**		JA (92)

Individualism (1980: 222)

01 – 10	11 – 20	21 – 30	31 – 40	41 – 50	51 – 60	61 – 70	71 – 80	81 – 90	91 – 100
	VN (12)		**PH (32)**	JA (46)		IR (70)	**DN (74)** **SW (71)**	AU (90)	US (91)

Masculinity (1980: 279)

01 – 10	11 – 20	21 – 30	31 – 40	41 – 50	51 – 60	61 – 70	71 – 80	81 – 90	91 – 100
SW (05)	**DN (16)**				AU (56)	IR (68) **PH (64)** US (62)	**VN (73)**		JA (95)

Values in parentheses are the actual cultural constructs.

AU	Australia	CH	China	DN	Denmark
IR	Ireland	JA	Japan	PH	Philippines
SW	Sweden	US	United States	VE	Venezuela

Fig. 1. Hofstede's Cultural Constructs by Country.

for SDRB such as the Marlow-Crowne scale (Crowne & Marlowe, 1960). While Randall and Gibson (1990) find that scores on the Paulhus significantly associate with scores on the Marlow-Crowne instrument, using the Marlow-Crowne instrument could provide an invaluable replication of our results.

The second limitation is that the sample comes from only five countries and may not be generalizable. We suggest that future researchers examine the cultural constructs (Hofstede, 1980) of the five countries in our sample and then test the generalizability of our findings on samples with markedly different cultural constructs. For example, an interesting extension of this research would be a study that includes countries, such as Denmark, the Philippines, Sweden, and Venezuela (Fig. 1 in bold print). The cultural constructs of Denmark and Sweden provide a sharp contrast to those of the Philippines and Venezuela.

NOTES

1. While we examine 20 studies since 1990, the Payne and Nantz (1994) (Borkowski & Ugras, 1998) study is a mega analysis of 22 (47) studies examining cheating between 1964 and 1991 (1985 and 1991).

2. The authors' university requires that students take a concentration of five liberal arts courses during their junior and senior years. One of the options to fulfill this requirement is to study abroad and take a "culturally oriented courses" (i.e., a concentration within a specific culture). As business courses would not count for the five-course concentration, the study abroad students are not part of the classes that participated in our questionnaire.

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APPENDIX A. SURVEY QUESTIONS BY CATEGORY

Questionable Academic Practices Questions (5-point Likert scale)

1. Looking at another student's exam during tests.
2. Using unauthorized ''crib'' notes during an exam.
3. Borrowing another person's speech, report, or paper and presenting it as one's own work.
4. Having someone else write a speech, report, or paper for you after you have done the basic research.
5. Rephrasing words or ideas from a book, journal, or magazine and presenting them without giving their source.
6. Asking someone who has already taken an exam what the questions are.
7. Asking someone for the answers during an exam.
8. Exchanging papers during an exam.
9. Writing a speech, report, paper, etc., for someone else.
10. Lying to an instructor about illness, etc., when an exam or assignment is due.
11. Failing to report grading errors when the professor has not approved ignoring errors in the student's favor.
12. Copying homework from another student.
13. Studying from someone else's notes without their approval.
14. Not contributing one's fair share in a group project for which all the members will be given the same grade.
15. Falsifying or fabricating a bibliography.
16. Visiting a professor after an exam with the sole intention of biasing one's exam grade.
17. Taking a test for a friend.
18. Obtaining a copy of the exam prior to taking it in class.
19. Obtaining an old test from a fraternity/sorority file or from a student who took the class in a previous semester when the professor has expressly prohibited the release of old tests.
20. Giving answers to someone else during an exam.
21. Turning in work or a paper purchased from a fellow student or a commercial research firm.
22. Arranging to sit next to someone in order to copy off that individual's test paper.
23. Bribing or blackmailing a fellow student or a professor to provide unauthorized assistance.

Deterrent value of possible punishment questions (5-point Likert scale)

1. Knowing that the order of the questions is scrambled on versions of a multiple choice test.
2. Knowing that the multiple choice answers as well as the questions were scrambled on versions of the test.
3. Giving problems/short answers/essay questions instead of multiple choice questions.
4. Knowing that the given information for problem/short answer questions is not the same on all test versions.

Cynicism questions (5-point Likert scale)

1. People who say they have never cheated before are hypocrites.
2. Everybody steals, cheats, or lies at least once in his/her lifetime.
3. People have to cheat in this "dog-eat-dog" world.

Personal experience questions (1–10 and 16–18 are Yes/No questions; 11–13 and 15 are multiple choice, 14 asks for an estimate; and 19–21 are short essays)

1. Have you ever observed another student cheating on an exam?
2. Have you ever observed another student cheating on a project or a written assignment?
3. Have you ever seen another student get caught cheating?
4. Do you know anyone who routinely cheats on exams?
5. Have you ever cheated on a major exam (20% or more of the final grade)?
6. Have you ever cheated on a minor exam (less than 20% of the final grade)?
7. Have you ever cheated on a major project or assignment (20% or more of the final grade)?
8. Have you ever cheated on a minor project or assignment (less than 20% of the final grade)?
9. Do you think you will cheat in the future?
10. Have you ever been caught cheating?
11. Based on your experience in large sections where multiple-choice testing is used, what percentage of students do you think cheat on a typical exam?
12. If you are caught cheating on an exam, what would you expect to happen?

13. If you are caught cheating on a project or written assignment, what would you expect to happen?
14. Of the cheating you have observed, what percentage do you think was "panic" cheating and what percentage do you think was "premeditated." While panic cheating is not planned, premeditated cheating is planned in advance of the test.
15. In your opinion, cheating at the university level is:
16. Do you think more should be done to stop cheating?
17. Do you believe cheating is a direct result of the competition for grades?
18. Do you believe cheating is wrong, dishonest, or unethical?
19. Describe the most common method of cheating you have observed in college.
20. Describe the most unusual or creative form of cheating you have observed in college.
21. What do you feel would be an effective way to deter cheating?

APPENDIX B. IMAGE MANAGEMENT SUBSCALE

Using the scale below as a guide, write a number beside each statement to indicate how much you agree with it.

1	2	3	4	5	6	7
Not True			Somewhat True			Very true

1. Sometimes I tell lies if I have to.
2. I never cover up my mistakes.
3. There have been occasions when I have taken advantage of someone.
4. I never swear.
5. I sometimes try to get even rather than forgive and forget.
6. I always obey laws, even if I'm unlikely to get caught.
7. I have said something bad about a friend behind his/her back.
8. When I hear people talking privately, I avoid listening.
9. I have received too much change from a salesperson without telling him or her.
10. I always declare everything at customs.
11. When I was young, I sometimes stole things.
12. I have never dropped litter on the street.
13. I sometimes drive faster than the speed limit.
14. I never read sexy books or magazines.

15. I have done things that I don't tell other people about.
16. I never take things that don't belong to me.
17. I have taken sick leave from work or school even though I wasn't really sick.
18. I have never damaged a library book or store merchandise without reporting it.
19. I have some pretty awful habits.
20. I don't gossip about other people's business.

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THE INTENTION OF ACCOUNTING STUDENTS TO WHISTLEBLOW IN SITUATIONS OF QUESTIONABLE ETHICAL DILEMMAS

Tara J. Shawver and Lynn H. Clements

ABSTRACT

The Sarbanes–Oxley act gives new protection to an individual who reveals wrongdoing in the corporate workplace. The public continues to demand more accountability by accountants, and the accounting profession is making strides to strengthen the integrity and the reputation of its professionals. Accounting students, the future of the profession, are the hope for a stronger and more ethical group of professionals. We attempt to identify the perceptions of justice, deontology, utilitarianism, relativism, and egoism that contribute to the intentions of accounting students to blow the whistle. We find, in general, that accounting students perceive the acts in these four vignettes as unethical; however, are less likely to whistleblow for acts relating to product safety and reducing bad debts and more likely to whistleblow for the acts relating to early shipments and unfair loans. We find at least one philosophical construct is perceived as significant for the intention to whistleblow for each vignette.

Well-known whistle-blowers Cynthia Cooper (WorldCom), Sherron Watkins (Enron), and Joe Speaker (Rite Aid) changed their organizations and, in

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doing so, changed their own lives. They each made the critical decision to blow the whistle on wrongdoing in their respective organizations. There are serious risks involved if one chooses to whistleblow. On one end, whistle-blowers could be praised as ethical and honored members of society, exposing wrongful acts improving society as a whole. On the opposite end, whistle-blowers could be seen as traitors of their own organizations and colleagues (Lennane, 1993; De Maria & Jan, 1994). One might ask, why did these individuals choose to whistleblow?

The public has always assumed accountants are honest. The fall of Enron Corporation in 2002 caused an almost perceptible gasp by the general public that accountants would act unethically and might look the other way as their clients did the same. Although the Certified Public Accountant (CPA) and Certified Management Accountant (CMA) certifications promote ethical behavior by requiring compliance with codes of ethics, incidents of accountants avoiding and ignoring known unethical acts continue to abound. Woolf (2004) states "imagine the healing effect on the public consciousness of a comparable act of facing responsibility ..." Whistle-blowing is the ultimate responsibility of an accountant.

The Sarbanes–Oxley Act increased the focus on whistle-blowing by including the requirement that public companies provide a channel for reporting corporate wrongdoing, and giving rights and protection to the whistle-blower. David Welch is the first whistle-blower to claim the protective provisions of the Sarbanes–Oxley Act (Telberg, 2004). A U.S. Department of Labor action dated January 28, 2004 (U. S. Department of Labor, 2004) reported that Welch was fired for reporting insider trading incidents by management of his employer, the Bank of Floyd (a subsidiary of Cardinal Bankshares Corporation). Section 806 of the Act prohibits a Securities Exchange Commission-registered company from discharging an employee for providing information about certain corporate wrongdoing. The preliminary findings gave Welch the right to recover his litigation costs and expenses, and to be reinstated as CFO.

Why might someone feel compelled to whistleblow? The answer to this question can help to promote the reporting of wrongdoing and thereby help to create a more ethical workplace. The provisions under Sarbanes–Oxley act grant whistle-blower protections; however, this does not necessarily mean that one would choose to whistleblow. The extensive whistle-blowing research covers a wide variety of topics, none of which has determined the underlying factors contributing to the decision to blow the whistle. We attempt to identify the factors of justice, deontology, utilitarianism, relativism, and egoism that contribute to the intention of our future professionals,

the accounting students, to blow the whistle. We investigate these factors using junior and senior accounting students. This research provides valuable insights into the attitudes regarding whistle-blowing. This research adds to the current stream of research by examining the whistle-blowing intentions of the future accountants and auditors, the accounting students. Further, studying accounting students provides an educational opportunity to expose students to whistle-blowing as a viable alternative to expose wrongful acts.

LITERATURE REVIEW

Whistle-blowers are those individuals who "sound an alarm from within the very organization in which they work, aiming to spotlight neglect or abuses that threaten the public interests" (Bok, 1980, p. 277). Hersh states that "whistleblowing involves the deliberate disclosure of information about non-trivial activities which are believed to be dangerous, illegal, unethical, discriminatory or to otherwise involve wrongdoing, generally by current or former organisation members" (Hersh, 2002, p. 243). Most definitions are not limited to illegality, and all include some type of reporting of questionable morality or wrongdoing.

Prior research has attempted to determine which employees blow the whistle. Past studies report personal characteristics (Miceli & Near, 1984; Miceli, Roach, & Near, 1988) and organizational variables (Miceli & Near, 1991) as contributing whistle-blowing factors. Greenberger, Miceli, and Cohen (1987) found group conformity to impede the whistle-blowing process. According to De Maria (1992), most whistle-blowers act on their own.

Barnett, Cochran, and Taylor (1993) found advantages to organizations when internal whistle-blowing is encouraged, appropriate changes are made, and external whistle-blowing is averted. Barnett suggests procedures for the development of internal disclosure policies, communication channels, investigative procedures, and protection vehicles for the whistle-blower in order to discourage external whistle-blowing. The factors reducing external disclosure include the incorporation of ethics in the corporate philosophy, a code of ethics and monitoring of the code, clear guidelines on unacceptable behavior, clear procedures for internal reporting (Winfield, 1994), and punishment for violations and effective whistle-blower protection (Benson & Ross, 1998). Miceli and Near (1985) found an increase in the likelihood of external whistle-blowing in a retaliatory climate.

Certain other self-regulating professions, such as medicine and engineering, implicitly encourage whistle-blowing through ethical codes of conduct. Perrow (1986) found that legislation acts too slowly to protect the public, suggesting engineers do hold their peers responsible for professional and ethical codes rather than waiting for legislation to right the wrongs. Whistle-blowing has effectively changed policy in the engineering industry over the years in the development of the anti-nuclear movement (Bernstein & Jasper, 1996; Nelkin, 1971; Jasper, 1990). In many cases, the effects included public awareness, debate over environmental issues, and threats of catastrophic accidents. The aim of a study by Ahern and McDonald (2002) was to identify beliefs that could be motivational factors for whistle-blowers in an attempt to explain why some people report misconduct and others do not. A study of 500 registered nurses in Australia indicates whistle-blowers support the beliefs inherent inpatient advocacy (i.e., nurses are primarily responsible to the patient and should protect the patient), while non-whistle-blowers believe in the traditional role of nursing (nurses have an obligation to follow a physician's order at all times, and are equally responsible to the patient, the physician, and the employer).

The engineering and nursing professions demand the reporting of wrongdoing because the wrongdoing often involves life and death issues. Although accounting wrongdoing rarely has a life or death result, the economic losses from the accounting scandals of the last years have had a profound effect on the financial and emotional health of the general public. This places upon the accounting profession a call by the public to a new level of integrity, and a responsibility to sound the alarm at the first sign of fraudulent accounting practices. Each accounting certification program has its own ethical code of conduct. Several, such as the CPA and CMA certifications, require consideration of unethical behavior, implicitly assuming the ability to recognize unethical acts. Statement on Management Accounting 1C (SMA 1C, 1997) of the Institute of Management Accountants (IMA, 1997) recognizes the potential problems of identifying unethical behavior or resolving ethical conflicts. SMA 1C instructs members of the IMA to follow the policies of the organization in reporting unethical behavior, and provides courses of action in the event those policies do not resolve the ethical conflict. According to Section 52 of the AICPA Code of Professional Conduct (AICPA, 1997), AICPA members "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." Section 53 specifically states that the public relies on the CPA "to

maintain the orderly functioning of commerce. This reliance imposes a public interest responsibility on certified public accountants.''

Using an analysis of 50 interviews with probation personnel, Rosecrance (1988) developed a model of the whistle-blowing event: (1) internal criticism of questionable activity and lack of reaction from superiors, (2) frustration at the lack of response, (3) external disclosure, (4) responses of the organization, and (5) the aftermath.

Near and Miceli (1995) propose a model linking five factors that influence the cessation of wrongdoing and five sets of moderating variables. The five factors influencing cessation of wrongdoing include: ''(a) characteristics of the whistle-blower, (b) characteristics of the complaint recipient, (c) characteristics of the wrongdoer, (d) characteristics of the wrongdoing, and (e) characteristics of the organization'' (Miceli & Near, 1985, p. 681). Of the five sets of moderating variables, three are based on the individual and two on the situation. Their model links perceived motives to the termination of wrongdoing.

Although limited, research related to whistle-blowing in an accounting or business context is developing as a result of accounting frauds. Chung, Monroe, and Thorne (2004) examined factors affecting external and internal whistle-blowing by auditors, finding individuals more likely to blow the whistle internally than externally, more likely to whistleblow where the organizational climate is principle-based as opposed to rule-based, and more likely to blow the whistle on a less powerful wrongdoer than a more powerful wrongdoer if the complaint recipient is within the organization. Xu and Ziegenfuss (2003) investigated the issue of whistle-blowing in the preparation of financial information. Their experiment examined whether reward systems impact auditors' whistle-blowing behavior. Based on their results, internal auditors are more likely to blow the whistle for a reward (i.e., cash or a continuing employment contract). Their results also indicate that those internal auditors with lower levels of moral reasoning are more sensitive to cash rewards than internal auditors with higher levels of moral reasoning. Brody and Bowman (1998) studied the effects of ethics education on accounting majors and psychology majors. The accounting majors were exposed to discussions of whistle-blowing and its ethical ramifications, while the psychology majors received no formal instruction in ethics. No significant differences resulted with respects to the ethical decisions made by the accounting and psychology majors. Lawson (2004) found that business students are reluctant to whistleblow for academic dishonesty or cheating.

Multi-dimensional Ethics Scale

The main ethical dilemma in blowing the whistle is the balancing of values, obligations to the organization, obligations to the general public, and an obligation to oneself (Jensen, 1987; Judd, 1999). The whistle-blower is faced with conflicting values between the right to privacy and the public's right to know (Devine, 1995). These values and obligations can be measured by the multi-dimensional ethics scale (MES). The MES allows researchers to identify several underlying factors when individuals choose to make decisions. Because there are no existing survey instruments that examine the factors that contribute to whistle-blowing behaviors in an accounting context, we adjust vignettes developed by Cohen, Pant, and Sharp (1993, 1996, 1998) by adding a question requesting the student to indicate their likelihood of blowing the whistle for each vignette. The Cohen et al. vignettes pose ethical dilemmas relating to accounting and business this allows us to measure a respondent's perceptions of justice, deontology, utilitarianism, relativism, and egoism. Once the student indicates whether or not they believe the action is ethical and whether or not they would whistleblow in each of these situations, we can attempt to identify which constructs are factors in their decisions. These constructs disclose the students' values, beliefs, and obligations in relation to their likelihood to blow the whistle for each vignette.

Four of the eight MES vignettes were selected for use in this study. Although all eight of the Cohen et al. vignettes are business related, we chose four vignettes most closely relating situations an accountant might face, to focus our study in this area and reduce time demands. Vignette product safety discusses a situation where a manager must decide whether to promote a product that has been insufficiently tested. The manager's decision to promote this product would increase sales and increase his commission. Vignette early shipment discusses a situation of an early shipment of product to meet a quarterly bonus. The decision to ship products early would also increase sales. Vignette unfair loan discusses a situation where a credit manager loans money to a friend that would not normally meet the lending criteria. Vignette bad debt discusses a situation where a controller adjusts an estimate for bad debt to increase reported income. Either directly or indirectly, each vignette has an impact to income reported on the financial statements. Each student indicates their belief of whether the action was ethical and whether they would complete each action on a 7-point Likert scale ranging from "ethical" to "unethical." Appendix A contains the four vignettes.

Prior studies conducted by Cohen et al. (1993, 1996, 1998), Cruz, Shafer, and Strawser (2000), Reidenbach and Robin (1990), and Sennetti, Shawver, and Bancroft (2004) found that many of these constructs influence decisions described in studies using their respective situational vignettes. Cohen et al. (1993, 1996) and Sennetti et al. (2004) found the constructs of justice, deontology, utilitarianism, relativism as significant underlying reasons that influence ethical decisions. Cruz et al. (2000) and Reidenbach and Robin (1990) found that the justice, deontology, and relativism were significant in their respective situational vignettes. These philosophical constructs help explain why someone believes an act is ethical or unethical and why they would or would not complete the action. We extend these constructs to help identify the underlying reasons of why someone would whistleblow. The benefit of an MES approach is that specific subtleties may exist in an ethical situation that changes the ethical judgment and behavior of an accountant. Just determining that an action is unethical may not be the only reason that someone would whistleblow. Therefore, we hypothesize the following:

H1. Accounting students identify philosophical constructs of justice, deontology, utilitarianism, relativism and egoism as reasons for whistleblowing.

METHODOLOGY

The questionnaire was administered to accounting students attending a small private Association to Advance Collegiate Schools of Business (AACSB) accredited educational institution. Each year, approximately 30 accounting majors graduate from this institution. Table I provides the demographic data. The entire junior and senior class of accounting majors participated in this study, consisting of 61 students. Fifty-four usable responses were obtained after incomplete surveys were eliminated from the study. The average age of these students is 24 years and the sample includes

Table I. Demographic Data.

N	54	100%
Seniors	31	57%
Juniors	23	43%
Males	28	52%
Females	26	48%
Average age	24	

28 males and 26 females. The sample indicates neither liberal nor conservative political views with an average of 2.91 on a scale from 1 "very liberal" to 5 "very conservative."

Each questionnaire was administered during class time with instructions on how to complete each section. Each student completed the anonymous survey and was informed that their participation is voluntary. Each survey contained the MES vignettes and the short version of the impression management (IM) scale. Paulhus (1991) developed the IM scale, which is a set of questions within the balanced inventory of desirable responding (BIDR). The IM questions are used to identify whether a student has answered questions in a manner that deliberately underreports socially undesirable acts. These questions include statements such as "When I hear people talking privately, I avoid listening." Each statement is rated on a 7-point Likert scale ranging from "not true" to "very true." For this study, the mean IM for males is 2.61 with a standard deviation of 2.42 and females scored 3.53 with a standard deviation of 3.02. Paulhus found typical scores for males to average 2.93 with a standard deviation of 2.8, for females to average 3.21 with a standard deviation of 2.8. These scores are not statistically different from the typical scores reported by Paulhus. This indicates that students have not provided socially biased answers.

RESULTS AND DISCUSSION

In Table II, we summarize the means and standard deviations for the evaluation of each ethical situation and the likelihood that the students will whistleblow. The means indicate that in all four vignettes the students believe that the action take in each vignette are unethical with scores ranging from 4.98 to 5.85 on a scale from 1 to 7 (1 as ethical, and 7 as unethical). Since the students have identified that each vignette is unethical, the next

Table II. Is It Ethical and Whistle-Blowing Means and Standard Deviations.

Vignette	Ethical (Mean)	SD	Whistle-Blow (Mean)	SD
Product safety	5.85	1.13	3.02	1.38
Early shipment	5.30	1.44	4.28	1.76
Unfair loan	4.98	1.38	4.28	1.70
Reduce bad debt	5.78	1.37	3.04	1.59

Note: 1 is ethical, 7 unethical, 1 whistleblow, 7 not whistleblow.

Table III. Ethical Intention and Evaluation.

Vignette	Do it? Mean	Do it? SD	Peers Do it? Mean	Peers Do it? SD
Product safety	5.28	1.62	4.06	1.65
Early shipment	4.45	1.76	3.75	1.86
Unfair loan	4.19	1.75	3.57	1.54
Reduce bad debt	5.37	1.62	4.65	1.59

Note: 1 do it, 7 not do it.

decision the student must face is to decide whether or not they would act as the person in the vignette did.

In Table III, we summarize the means and standard deviations for the ethical intention of whether the student and their peers would complete the act. The means for "the probability that I would undertake the same action" ranges from 4.19 to 5.37 (1 complete the act, 7 would not complete the act). These means indicate that these students are less likely to complete the act. The means for "the probability that my peers would undertake the same action" ranges from 3.57 to 4.65. Once the student has identified an unethical situation and has indicated they would not to complete the act, the next decision is to decide whether or not they intend to blow the whistle.

The means for the intention to whistleblow ranges from 3.02 to 4.28 ranging on a scale from 1 to 7 (1 being a low likelihood to whistleblow and 7 being a high likelihood to whistleblow). This lower range indicates less likelihood to whistleblow for acts relating to product safety and reducing bad debts, and more likelihood to whistleblow for acts relating to early shipments and unfair loans. The next step is to determine what factors contribute to the likelihood of whistle-blowing.

For H1 a regression between the intention to whistleblow and the constructs of the MES identifies that accounting students identify at least one of the MES constructs (justice, deontology, utilitarianism, relativism, and egoism) as reasons for whistle-blowing. The adjusted R^2 for each vignette are product safety 0.138, early shipment 0.247, unfair loan 0.181, and bad debts 0.265. The adjusted R^2 in Table IV confirms that the underlying constructs of justice, deontology, utilitarianism, relativism, and egoism had varying impacts in each vignette. However, all four vignettes identified the perception of justice as a significant factor in determining the intent to whistleblow. The construct of justice deals with a respondent's feeling that all people should be treated equally. Although prior research has not examined the underlying reasons of whistle-blowing, the finding that justice influences ethical judgments is consistent with prior studies by Cohen et al.

Table IV. Whistleblowing Intention and the Components of the Multidimensional Ethics Scale.

Vignettes	MES and Whistleblow Adjusted R^2	Components of the MES			(Statistical p-values)[a]	
		Justice	Relativism	Egoism	Utilitarianism	Deontology
Product safety	0.138 (0.032)*	2.05 (0.045)*	1.71 (0.094)*	0.27 (0.786)	−0.93 (0.355)	0.11 (0.915)
Early shipment	0.247 (0.002)*	1.895 (0.064)*	0.45 (0.655)	0.58 (0.564)	1.75 (0.087)*	0.81 (0.420)
Unfair loan	0.181 (0.012)*	2.08 (0.043)*	1.912 (0.062)*	−0.049 (0.961)	0.632 (0.530)	−0.757 (0.453)
Bad debt	0.265 (0.001)*	3.55 (0.001)*	0.62 (0.540)	−0.94 (0.352)	0.24 (0.809)	−0.71 (0.479)

*Statistically significant for p-values <0.05 and moderately significant for p-values <0.10 but >0.05.

[a]All p-values are computed from two-tailed t tests.

(1993, 1996), Reidenbach and Robin (1990), Cruz et al. (2000), and Sennetti et al. (2004). The construct of relativism identifies that each culture has differing rules and regulations that are acceptable within that culture. Relativism is significant for product safety and unfair loan. The construct of utilitarianism identifies that all decisions have expected costs versus benefits. Utilitarianism is significant for early shipment. Cohen et al. (1996) found similar results for the construct relativism in explaining the action in product safety and unfair loan, in addition to early shipment, and bad debts. The construct of egoism deals with decisions based on one's own self-interest. Consistent with prior studies by Cohen et al. (1993, 1996), Cruz et al. (2000), and Sennetti et al. (2004), no egoism factor was significant in this study. The construct of deontology deals with duty and one's feelings of implied contracts with society. The deontology factor was not significant in this study, this is not consistent with prior studies.

For each vignette, an open-ended question provided an opportunity for students to write a response supporting why they may feel the action is either ethical or unethical. These responses provide more insights into why a student may or may not whistleblow. Recall that all four vignettes had means ranging from 4.98 to 5.85, indicating that these actions generally are considered to be unethical. The product safety vignette had a mean score of 3.02 for the likelihood of whistle-blowing, with 1 indicating a low likelihood of whistle-blowing and 7 a high likelihood of whistle-blowing. Several students indicated that the company had an obligation to fully test products

prior to marketing them, while other students indicated that it is not necessarily the sales manager's responsibility to determine if proper testing has occurred. This lack of perceived responsibility for the product manager may be a reason why product safety was one of the two vignettes where whistle-blowing is less likely. These responses show some concern for the justice and relativism constructs. For reducing bad debts, justice was the only significant construct, and the mean score for whistle-blowing was 3.04 with several students indicating that the action of reducing the bad debts was unethical using words such as "fraud" or "misleading shareholders." Although some students believed that recent earnings management manipulations by accountants are inappropriate, other students indicated that since other companies or managers are doing it, the practice of earnings management has become acceptable. This acceptance of earnings management may hinder the likelihood for whistle-blowing. Both acts relating to early shipments and unfair loans had a mean score of 4.28 indicating more likelihood to whistleblow. Several students indicated that even though the credit manager is helping a friend, the loan is unfair to others who meet the lending criteria. These responses are consistent with the justice and relativism constructs that were shown to be significant in the regressions. For early shipments, some students indicated that this action would be ethical if the company had approved an early shipment; however, managing the numbers is believed to be unethical and only in the managers' interest to do so. These responses are consistent with the justice and utilitarianism constructs.

These insights into the underlying reasons for whistle-blowing are important to the accounting profession. This information can be used by academics in training future accounting professionals, by companies as a starting point to understanding whistle-blowing behaviors, by upper management and audit committees as a potential effective management tool, and by regulators in setting corporate governance regulations.

CONCLUSIONS

Literature in the whistle-blowing area has concentrated on whether or not whistle-blowing is ethically right, whether ethics training impacts the decision to blow the whistle, the characteristics of whistle-blowers, and the channels whistle-blowers use to report wrongdoing.

Whistle-blowing options are becoming more known as recent accounting scandals are publicized in the media. Cynthia Cooper (Worldcom), Coleen Rowley (FBI), and Sherron Watkins (Enron) were hailed as *Time Magazine*

Persons of the Year for their actions as whistle-blowers. We recognize that the decision to whistleblow involves a balancing of values, and this study attempts to determine what factors contribute to the decision that would cause someone to blow the whistle starting with the identification of an unethical act and leading to the underlying reasons of why someone may whistleblow. We find, in general, that the accounting students used in this study perceive the acts in these four vignettes as unethical. However, the accounting students are less likely to whistleblow for acts relating to product safety and reducing bad debts, while more likely to whistleblow for acts relating to early shipments and unfair loans. We find the perceptions of the philosophical constructs of justice, deontology, utilitarianism, relativism, and egoism had varying impacts in each vignette; however, at least one philosophical construct is perceived as significant in each of the four accounting and business-related vignettes.

Although this study contributes to the literature, there are limitations that must be noted. This is a study conducted on accounting juniors and seniors from one small AACSB accredited educational institution; therefore, sample size and regional differences limit this study. In the wake of Sarbanes–Oxley, future researchers may wish to examine the effectiveness of whistle-blowing protection legislation, internal programs encouraging whistle-blowing, and the long-term career effects on whistle-blowers whose names have been made public. In addition, the importance of factors, such as the severity of the wrongdoing and the possible interaction of situational and personal factors (consequences, rewards, ethical issues, and loyalty conflicts) could be studied. More research is needed to identify the ways that we can change unethical behaviors into more socially responsible behaviors. Clearly, accounting as a profession may wish to explore the intentions of working professionals to provide feedback to explain the moral judgments and whistle-blowing intentions of accounting professionals.

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APPENDIX A

Vignette Product Safety. A company has just introduced a highly successful new kitchen appliance. The sales manager, who is paid partly on a commission basis, discovers that there has been insufficient product testing to meet government guidelines.

The tests so far indicate no likelihood of any safety problem.

Action: The sales manager continues to promote the product.

Vignette Early Shipment. A manager realizes that the projected quarterly sales figures will not been met, and thus the manager will not receive a bonus. However, there is a customer order which if shipped before the

customer needs it will ensure the quarterly bonus but will have no effect on the annual sales figures.

Action: The manager ships the order to ensure earning the quarterly sales bonus.

Vignette Unfair Loan. A promising start-up company applies for a loan at a bank. The credit manager at the bank is a friend of and frequently goes golfing with the Company's owner. Because of this company's short credit history, it does not meet the bank's normal lending criteria.

Action: The credit manager recommends extending the loan.

Vignette Bad Debt. The CEO of a company requests to the controller to reduce the estimate for bad debts in order to increase reported income, arguing that this is common practice in the industry when times are hard. Historically, the company made very conservative allowances for doubtful accounts, even in bad years. The CEO's request would make it one of the least conservative in the industry.

Action: The controller makes the adjustment.

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AN INSTRUCTIONAL CASE IN PREMATURE REVENUE RECOGNITION

Steven M. Mintz

"We can't recognize revenue immediately, Paul, since we agreed to buy similar software from Data Systems Solutions." "That's ridiculous," replied Paul. "Get your head out of the sand, Sarah, before it's too late."

Sarah Young is a certified public accountant (CPA) and the controller for Solutions Network, Inc. She is meeting with Paul Henley, the chief financial officer of the company, on January 7, 2006, to discuss the accounting for a software systems transaction with Data Systems Solutions (DSS) prior to the company's audit for the year ended December 31, 2005. Henley is not a CPA.

Sarah has excluded the amount from revenue and net income for 2005. Paul wants the amount to be included in the 2005 results. Paul told Sarah that the order came from the top to record the revenue on December 28, 2005, the day the transaction with DSS was finalized. Sarah pointed out that Solutions Network ordered essentially the same software from DSS to be shipped and delivered early in 2006. Therefore, Solutions Network should delay revenue recognition until that time. Paul argued against her position stating that title had passed from the company to DSS on December 31 when the software product was shipped with F.O.B. Shipping Point terms.

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BACKGROUND

Solutions Network, Inc. became a publicly owned company on March 15, 2005, following a successful initial public offering (IPO). Solutions Network built up a loyal clientele in the previous five years by establishing close working relationships with technology leaders including IBM, Apple, and Dell Computer. The company designs and engineers system software to function seamlessly with minimal user interface. There are several companies that provide similar products and consulting services. One is DSS. However, DSS operates in a larger market providing IT services management products that coordinate the entire business infrastructure into a single system.

Solutions Networks grew very rapidly in the five years prior to its IPO. The revenue and earnings streams during those years are as follows.

	(In millions)	
Year	Revenues	Net income
2000	148.0	11.9
2001	175.8	13.2
2002	202.2	15.0
2003	229.8	16.1
2004	267.5	17.3

Sarah has prepared the following estimates for 2005.

	(In millions)	
	Revenues	Net income
2005 (projected @ 12/31)	287.5	17.9

THE TRANSACTION

On December 28, 2005, Solutions Network offered to sell its Internet infrastructure software to DSS for its internal use. In return, DSS agreed to ship similar software 30 days later to Solutions Network for that company's internal use. The companies had conducted several transactions together during the previous five years and while DSS initially balked at the transaction because it provided no value added to the company, it did not want to upset one of the fastest growing software companies in the industry.

Moreover, Solutions Network could help to identify future customers for DSS's IT services management products.

The $30 million of revenue would increase net income 1.9 million over the projected amount for 2005. For Solutions Network, the revenue from the transaction was enough to enable the company to meet targeted goals and the higher level of income would provide extra bonus money at year-end for Sarah Young, Paul Henley, and Ed Fralen, the chief executive officer.

ACCOUNTING CONSIDERATIONS

Normally, Sarah would not object to Paul's proposed accounting for the transaction with DSS. However, she knows that regardless of the passage of title to DSS on December 31, 2005, the transaction is linked to Solutions Networks' agreement to take the DSS product 30 days later. Sarah does not anticipate that being a problem. Still, she is uncomfortable with the recording of revenue on December 31 since DSS did not complete its portion of the agreement by that date.

Sarah is also concerned about the fact that last year another transaction had occurred that she questioned but, in the end, Sarah went along with the accounting. On December 28, 2004 Solutions Network sold a major system for $20 million to Laramie Systems but executed a side agreement with Laramie on December 29, 2004, that gave the customer the right to return the product for any reason after January 1, 2005, and for 27 additional days. Even though Solutions Network recorded the revenue on December 29, 2004, and Sarah felt uneasy about it, she did not object because Laramie did not return the product. Sarah never brought it up again. Now, she is concerned that a pattern may be developing.

QUESTIONS

1. Describe the rules in accounting for revenue recognition in general and relate them to the two transactions mentioned in the case. Be sure to include proper citations from the pronouncements of the Financial Accounting Standards Board (FASB) and other relevant material. Do you believe the transactions have been accounted for properly?
2. (a) Prepare a schedule of the percentage of net income to revenues from 2000 through the projected amounts for 2005. Use the original amounts reported including 2004 and show the percentage changes in revenue and net income each year. In addition to the above, include in your schedule

the relevant amounts assuming: (1) The company restates the results for 2004 and (2) Solutions Network records the $30 million transaction with DSS in 2005 but does not correct the 2004 results.

(b) Now assume the corrected amounts for 2004 are used for comparison. (3) Show the percentage changes for 2005 using the original projected amounts including the effects of the correction of the Laramie Systems transaction.

3. Redo the comparative analysis using 2003 as the base year to show the effects on comparative revenues and net income from 2003 through 2005 assuming: (1) Solutions Network is allowed to record revenue for 2004 and 2005 the way it wants and (2) The company follows GAAP rules for recording revenue in both years. Comment on the results of your percentage analyses in questions (2) and (3). What do you think may have been the underlying motivation for Paul Henley and Ed Fralen to record revenue in the manner described in (1) above?
4. Assume Sarah meets with Paul on January 14, 2006, to finalize the accounting for the DSS revenue. Sarah asks Beth, her best friend, for advice. Beth is a CPA and has worked for a large international firm for many years. Therefore, you can assume Beth is knowledgeable about revenue recognition rules and other relevant principles. Prepare a draft of the recommendation you will make to Sarah that outlines the ethical issues, alternatives, and a recommended course of action. Be sure to support the recommended course of action with ethical reasoning.
5. Regardless of your answer to question (4), assume Sarah asks for more time to consider the matter when she meets with Paul on January 14. She points out that the auditors will not arrive until February 1, 2006; therefore, the company should be certain of the appropriateness of its accounting before that time. Paul reacts angrily and tells Sarah she can pack her bags and go if she doesn't support the company in its revenue recognition of the DSS transaction. Assume you are in Sarah's position. What virtue considerations exist that might help you to decide on a course of action? What would you do and why?

TEACHING NOTES

Objective of the Case and Discussion Questions

The primary purpose of the case is to provide a vehicle for students to read and interpret unstructured information dealing with revenue recognition.

Additionally, the case presents a financial reporting problem that has become all too common in the business world.

The way a transaction is accounted for relates to the ethics of those responsible for the accounting and reporting. In that regard, it is helpful for students to have a background in ethical reasoning to evaluate the dilemma in the case that exists because of a difference of opinion about how best to account for the transaction, and the related threat to Sarah Young.

The facts of the case mirror many of the events that occurred in the accounting scandals during the late 1990s and early 2000s.[1] It realistically presents the kind of situation a CPA might face when pressured by a superior to overlook proper accounting. In discussing the situation with students, it might be helpful to make the analogy with sliding down an ''ethical slippery slope.'' Once a person starts down that path, it is very difficult to turn back and reverse course. The key is not to take the first step.

Classroom Use of the Case

The case was tested in an Intermediate Accounting II class in spring 2005, after the coverage of the revenue recognition chapter. One class period (three hours) is devoted to discussing how to reason ethically. Since most of the students have completed either a philosophy of ethics and/or a business ethics course prior to the Intermediate II class, the discussion serves as a review of the philosophical reasoning methods. The following is a brief overview of what is discussed.

Students are told to access from the internet the material on ethical decision making published by the Markkula Center for Applied Ethics at Santa Clara University (www.scu.edu/ethics/practicing/decision/framework/html). A framework for ethical decision making is described and virtue ethics is discussed in class. The framework includes: (1) How to recognize there is an ethical issue; (2) What are the relevant facts of the case? (3) Who are the stakeholders and what are the decision maker's obligations to them? (4) Identify the alternative courses of actions; (5) Evaluate the alternatives using ethical reasoning and virtue considerations; and (6) Decide on a course of action and, if possible, discuss it with a trusted advisor.

The ethical reasoning methods are applied using the following perspectives: (1) Which option will produce the most good and do the least harm? (2) Which option respects the rights and dignity of all stakeholders? Even if some stakeholders may not get all they want, will all the stakeholders be treated fairly? (3) Which option would promote the common good and help stakeholders to participate more fully in the allocation of

resources? (4) Which option encourages virtue or the character traits that individuals in society and CPAs as accounting professionals should strive to achieve?

Each student in the class hands in written responses to the questions. Before the papers are graded and returned, the students are divided into four groups of four students. Each group has one hour to meet, discuss one of the first four questions that have been assigned to the group, and then present the group's response in class. Each group also must include in its remarks a separate response to the dilemma faced by Sarah as explained in the last question. A role-play situation can be used to discuss this question with students. Role-playing fosters reflective thought and forces student to think on their feet. One class period of 75 minutes is devoted to the presentations (15 minutes for each group; 15 minutes for questions).

The written papers and class discussions are 20 percent of the final course grade. This assignment replaces a term paper that had been given in the past. Students seem to enjoy the case project and benefit from it as comments indicate in the course evaluations. Comments include: "I learned and retained more by working with classmates"; "I now better understand the problems and potential abuses in revenue recognition"; and, my favorite comment: "I did more research on question one than I did last semester when I took the course with Professor (deleted) and failed the course."

Revenue recognition is critical to proper income determination. The issue is discussed in a variety of courses in addition to Intermediate Accounting. In the fall 2005 it will be used in a new course titled "Corporate Governance Systems," an undergraduate seminar that combines issues of ethics, financial reporting, and corporate governance. Undergraduate auditing courses and graduate seminars also provide excellent opportunities to go beyond the typical classroom discussion of revenue recognition in accounting and introduce students to the difficulty of revenue recognition and the concept of earnings management.

Extending the Boundaries of the Case

Additional FASB standards can be integrated into the discussion of question (1). In addition to EITF 93-11, Statement of Financial Accounting Standards (SFAS) No. 48, *Revenue Recognition When Right of Return Exists* (www.fasb.org), provides an opportunity to discuss how some criteria can be managed to achieve a desired result. Under SFAS 46, there are six criteria that must be met for an enterprise that sells a product with the right of

return to recognize revenue at the time of sale. These include:

a. The seller's price to the buyer is substantially fixed or determinable at the date of sale.
b. The buyer has paid the seller, or the buyer is obligated to pay the seller and the obligation is not contingent on resale of the product.
c. The buyer's obligation to the seller would not be changed in the event of theft or physical destruction or damage of the product.
d. The buyer acquiring the product for resale has economic substance apart from that provided by the seller.
e. The seller does not have significant obligations for future performance to directly bring about resale of the product by the buyer.
f. The amount of future returns can be reasonably estimated.

Students might be asked whether these criteria apply to the Laramie Systems transaction. The important point is that while it may appear on the surface to be applicable, the facts of the Laramie transaction are not the same as envisioned in SFAS 48. The Laramie transaction includes a side agreement for the return of the product rather than the anticipated return in the natural course of business. On a practical level, the determination of any estimated return as required by the sixth criterion may be virtually impossible thereby negating the possibility of immediate revenue recognition under the standard.

Motivation for the Case

The financial statement manipulations in companies such as Enron, WorldCom, Tyco, and Adelphia have been well publicized. However, the revenue recognition issues that existed in companies like Qwest and Global Crossing have not been well documented in discussions and cases in accounting. The so-called "roundtrip" or "swap" transactions, that really are barter transactions, were common to companies such as Qwest and Global Crossing. Sometimes these companies transacted with Enron and WorldCom on these deals. These transactions provide an opportunity to discuss the techniques a company might use to manage its earnings by managing the terms of a transaction.

Qwest Communications International Inc. agreed to a SEC consent order (www.sec.gov/litigation/lireleases/lr18936.html) to restate its revenue by $3 billion for the years 1999 through 2002. The company had sold "indefeasible rights of use (IRU)" to customers that enabled them to exchange telecommunications network capacity purchased from Qwest by transferring a similar amount of capacity back to Qwest in the future. Often, these arrangements

were executed as side agreements and hidden from Qwest's accountants and auditors. The original transaction was recorded as immediate revenue whereas the return transaction executed by Qwest when it agreed to take back similar capacity was accounted for as an asset and written off over a number of years. Not only were the revenue recognition rules violated by the immediate recognition (with an undisclosed side agreement) but the matching principle was completely ignored in the capitalization of the reverse side of the transaction.

While the facts in the instructional case differ from that of Qwest, the question is the same: When should revenue be recognized in a barter (swap) transaction and how do side agreements change that recognition? An important point is that the economic substance of such transactions should be placed ahead of any structural (legal) form in determining proper recognition. The Solutions Network case illustrates an important point for students. That is, it is ultimately the role of accountants and auditors to use professional judgment and apply ethical reasoning in determining the proper accounting for transactions regardless of the agreed treatment of the parties.

Suggested Responses

1. Statement of Financial Accounting Concepts No. 5 (CON5), *Recognition and Measurement in Financial Statements of Business Enterprises* (www.fasb.org), provides guidance in applying criteria to the recognition of revenue. Recognition involves the recording or incorporating of an item in the financial statements as an asset, liability, revenue, expense, gain, or loss. CON5 establishes guidelines to be followed in resolving issues that involve accounting recognition.

CON5 guidelines provide help to assess whether revenue exists and the proper amount to record before it is recognized. Revenues are generally measured by the exchange values of assets (goods or services) or liabilities involved, and recognition involves consideration of two factors that may vary in their importance depending on the situation. These include being realized or realizable and being earned.

Realized or realizable. Revenues should be recognized when realized or realizable. Realization occurs when products (goods or services), merchandise, or other assets are exchanged for cash or claims to cash. Revenues are realizable when related assets received or held are readily convertible to known amounts of cash or claims to cash. Convertibility requires that the assets have interchangeable units and quoted market prices exist to rapidly absorb the quantity held by the entity without significantly affecting the price.

Earned. Revenues are not recognized until earned. The revenue-earning flow depends on when the goods are produced or delivered, services rendered, or other activities that constitute the entity's ongoing major or central operations. Additionally and of particular concern in software sales, revenues are considered to have been earned when the entity has substantially accomplished what it must do to be entitled to the benefits represented by the revenues.

Qwest Communications fraudulently manipulated revenue through internet swap transactions. The consent agreement with the SEC includes the following admission:

> Qwest ignored generally accepted accounting principles (GAAP) by recognizing upfront revenue from IRU transactions and equipment sales ... [employing] fraudulent devices such as backdated contracts and secret side agreements to conceal the fact that its IRU and equipment transactions did not meet GAAP's requirements for upfront revenue recognition. Under GAAP, Qwest should either have not recognized any revenue on these transactions or recognized revenue ratably over the lives of the contracts.

The DSS transaction appears to be a sham that inappropriately inflates revenue and earnings. Solutions Network should defer revenue on its "sale" transaction with DSS since Solutions Network is obligated to "acquire" a similar product from DSS in 2006. Once that transaction is completed, Solutions Network should match the expense to acquire the infrastructure software from DSS with revenue because revenues are not earned by Solutions Network until it transfers its software product to DSS.

The sale transaction with Laramie Systems that includes a side agreement to return the product for full credit after year-end December 31, 2004, reflects an agreement used by some internet companies in the late 1990s and early 2000s to prematurely recognize revenue. For example, the demise of Informix Corporation in 1997 resulted in part from the disclosure that the company had improperly recorded $311 million in revenue on barter transactions ($140) and transactions executed with side agreements ($171 million). The latter are similar to transactions developed by Solutions Network.

One goal of transactions with side agreements is to record revenue before the end of a quarter or at year-end to meet internal budget estimates or financial analysts' estimates of earnings. The problem is that the company has borrowed from the future to meet current revenue needs and now has a shortfall to make up at the later date. Moreover, this kind of thinking becomes contagious, like a virus, and can lead to more and more manipulation of earnings. The result is that an unethical environment is

established; one that breeds focusing on short-term results rather than emphasizing proper accounting and long-term ethical action.

The revenue from Laramie Systems is not earned by Solutions Network until the return period expires. The earning process is not complete until that time. Unlike the return of a defective product in the normal course of business that can be estimated in advance, Laramie Systems had carte blanche to return the Solutions Network product.

2. Comparison of Increases in Revenues and Net Income with and without Adjustments (in Millions).

Year	Revs	% Incr in Revs	Net Inc	% Incr in NI	% NI to Revs
(a)					
2000	148.0	—	11.9	—	0.084
2001	175.8	0.188	13.2	0.109	0.075
2002	202.2	0.150	15.0	0.136	0.074
2003	229.8	0.136	16.1	0.073	0.070
2004	267.5	0.164	17.3	0.075	0.065
2004 (*with correction*[2])	247.5	0.077	16.7	0.037	0.067
2005 (proj. @12/31)	287.5	0.075	17.9	0.035	0.062
2005 (with 30 M[3])	317.5	0.187	19.8	0.145	0.062
(b)					
2005 (with 20 M[4])	307.5	0.242	18.5	0.108	0.060

[2]Italics denotes the corrected results for 2004 that excludes the $20 M.
[3]Bold denotes the results for 2005 with the $30 M included.
[4]Bold and italics represents the results for 2005 under GAAP including the inclusion of the $20 M revenue in 2005 and excluding the $30 M.

3.(1) Comparison of Increases in Revenues and Net Income: Company View (in Millions).

Year	Revs	% Incr in Revs	Net Inc	% Incr in NI	% NI to Revs
2003	229.8	—	16.1	—	0.070
2004	267.5	0.164	17.3	0.075	0.065
2005	317.5	0.187	19.8	0.145	0.062

3.(2) Comparison of Increases in Revenues and Net Income: GAAP View (in Millions).

Year	Revs	% Incr in Revs	Net Inc	% Incr in NI	% NI to Revs
2003	229.8	—	16.1	—	0.070
2004	247.5	0.077	16.7	0.037	0.067
2005	307.5	0.242	18.5	0.108	0.060

It appears Paul and Ed were motivated by the desire to smooth net income over time and, perhaps, provide higher bonuses to top management. If stock options had been outstanding, another motivation may have been to inflate earnings so that the stock price would go up (presumably), and then top management could cash in on the options. This was a common situation in frauds such as Enron and WorldCom.

The desired results show a steady increase in amounts between 2003 and 2005 with a marked increase in net income in 2005, and that increases the base for bonuses. If the company had followed GAAP, the results would show significant decreases in revenue and net income in 2004 as a percentage of the 2003 amounts while the 2005 comparative results would show substantial increases. Typically, top management seeks to report a steady growth in operating results to keep the stock price high. If Solutions Network had followed GAAP, it might be that investors would sell off stock in 2004 because the results indicate smaller percentage increases in revenues (0.077) and net income (0.037) over 2003 then is reflected by increases in the amounts for revenue (0.136) and net income (0.073) in 2003 when compared to 2002.

4. *Ethical Issues*. The accounting issues previously mentioned have ethical implications because CPAs are expected to follow GAAP in preparing financial statements and maintain their integrity. Indeed, it is a violation of the AICPA Code of Professional Conduct to be associated with statements that a CPA knows (or should know) do not conform to GAAP. Therefore, Sarah Young would violate her ethical obligations to the profession and key stakeholders if she goes along with the improper accounting for the $30 million transaction with DSS.

The investors and creditors expect financial statement information to be reliable and assist in their decision making. If Sarah goes along with the inflated numbers for 2005, then any decisions made by the stakeholders will be based on false and misleading information. The result is a breakdown in

the trust that should exist between accountants and their superiors and auditors and clients.

The revenue side of the transaction is negated by the acquisition of similar infrastructure software from DSS in 2006. In reality, there should be no net income effect of the barter transaction. Sarah seems to see through the sham and should stand up for what she knows is right. Integrity requires that a CPA should not subordinate professional judgment to others. Sarah violates the standard if so goes along with the improper accounting. She should bring her concerns to higher-ups in the company including the audit committee of the board of directors.

More harm than benefit will come to the stakeholders if Sarah goes along with Paul. Paul may believe that greater benefits will accrue to the company because the smooth earnings trend might help to increase the company's stock price and that could lead to higher bonuses for himself, Ed Fralen, and Sarah. Paul would be following an egoistic approach to decision making if this course is followed. It may be in the interests of those in top management, but it is not in the public interest. Moreover, the company risks its reputation, and Sarah risks her own reputation if she stands idly by while earnings are manipulated.

It is unethical to rationalize an action (that is wrong) by citing perceived financial or other benefits to certain stakeholders. An action is wrong because it fails to respect the rights of stakeholders and does not meet ethical requirements. In this case, the virtue of honesty requires that the statements should not be manipulated in a way that is designed to promote one's self-interests, but in the end deceives others along the way.

Alternatives. Sarah's alternatives are limited. She can go along with Paul and say nothing about the improper accounting or she can refuse to go along with the sham transaction.

The company is publicly owned and would have an audit committee consisting of independent members of the board of directors. Sarah could approach the audit committee and solicit its support in dealing with Paul. If the audit committee instructs Paul to account for both the DSS and Laramie transactions in accordance with GAAP, then Sarah will have won the battle with Paul. The unfortunate reality is that she still may lose the war since Paul could fire her shortly after meeting with the audit committee.

CPAs are expected to serve the public interest above all other interests including those of an employer, a client, and self-interests. This is a difficult standard to live up to in performing professional accounting services. The standard exists because the public relies on the objectivity of CPAs and has a right to expect truthful and nondeceptive financial information.

Recommendation. Sarah should seek out the support of the audit committee. Also, she should document her discussions with Paul Henley and the positions taken on the accounting issues. This approach is recommended by the Institute of Management Accountants in its standards of ethical conduct (www.imanet.org).

5. Virtues are traits of character that support ethical behavior. The virtue of honesty precludes both intentional misrepresentation of fact and the deliberate slanting of information. Integrity requires that CPAs should not subordinate their professional judgment to that of a supervisor or client. A CPA needs both the desire to act ethically and the courage to withstand pressures from a supervisor or client that might mitigate against taking ethical action.

Sarah should refuse to go along with Henley's proposed accounting for the DSS transaction. In the end, Sarah will be better off taking a strong stand now rather than going along with Paul. Typically, once a company starts to manipulate revenue and net income in one year it continues doing the same in the future because the company needs to keep up the appearance of growth. As the numbers in the response to 3.(b) indicate, if the company had not recorded the $20 million transaction with Laramie Systems as revenue in 2004, and reported it instead in 2005 as required by GAAP, then the "need" would not have existed to record the $30 million DSS transaction as revenue in 2005.

On a practical level, the danger of going along with Paul now is that in the future he might pressure Sarah on a different accounting issue and it would be more difficult for her to refuse. Paul might remind Sarah that she went along with inappropriate accounting in the past. Paul might make a veiled threat to use it against Sarah if all of a sudden she develops a conscience.

The pressure applied by Paul tests Sarah's commitment to do the right thing. The key is whether she has the moral courage necessary to follow her conscience.

NOTE

1. The transaction is a barter exchange. The $30 million amount of revenue would be determined under GAAP. The Accounting Principles Board (APB) and FASB's Emerging Issues Task Force (EITF) have noted that barter transactions should generally be recorded at the fair value of the assets surrendered. The challenge is to determine this amount. This issue is not dealt with in the case to focus student attention on the basic revenue recognition concepts and ethics issues. Faculty who choose to discuss the barter nature of the transaction should refer to EITF 93-11.

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CASE STUDIES FOR INTRODUCTORY TAX: INTEGRATING RESEARCH AND ETHICS

Cynthia E. Bolt

ABSTRACT

The introductory tax student faces an array of challenges, from complicated technical issues to overwhelming volume and countless exceptions to each complex law. Instructors face the challenge of teaching in one of the most difficult topics in accounting, where they must educate students about the delicate balance required to cope with the incongruent relationship between client and taxing authority. Educational frameworks, stressing the need for inclusion of a myriad of skills besides content, present additional pressures on the time-constrained instructor to include ethics, oral and written communication, research, and general business skills in their curriculum. This teaching case of four separate scenarios provides students with the opportunity to research a specific tax issue, use their professional judgment to interpret gray areas guided by the newly revised ethical standards, and communicate their findings in a professional format. The condensed format of the cases allows the instructor to cover a multitude of competencies using limited class time.

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CASE STUDIES FOR INTRODUCTORY TAX: INTEGRATING RESEARCH AND ETHICS

The introductory tax class creates challenges for even the most motivated faculty and student. Complicated technical issues, overwhelming volume, and countless exceptions to each complex law frustrate the student. A new language must be mastered with its own unique vocabulary: AGI, AMT, MFJ, "exemptions," "exclusions," "itemized deductions," "non-refundable credits." Instructors face the challenge of teaching one of the most difficult topics in accounting, where they must educate students about the delicate balance required to cope with the incongruent relationship between client and taxing authority. Educational frameworks, stressing the need for inclusion of a myriad of skills besides content, present additional pressures on the time-constrained instructor to include ethics, oral and written communication, research, and general business skills.

The accounting education frameworks of the 1980s and 1990s recommend a curriculum containing broad-business skills and concepts, analogous to the 2004 content modifications in the computerized Certified Public Accountant (CPA) exam (Bolt & Foster, 2003). The American Institute of Certified Public Accountants (AICPA's) Model Tax Curriculum recommends less tax compliance and more research, planning, and business integration. Hite and Hasseldine (2001) also advocate less content-specific lectures in college curriculum in favor of a broader look at the "accounting, financial and economic consequences" of the discipline.

Educators have begun to address the need for an ethical focus as advocated in American Accounting Association (AAA) (1986) Bedford Report and Accounting Education Change Commission (AECC) (1990) (Grasso & Kaplan, 1998; Finn, Chonko, & Hunt, 1988). Ethical problems in public accounting combined with the many recent corporate failures validate this need for curriculum modification. Yet, few schools offer individual ethics courses, particularly for accounting students, preferring instead to integrate their ethical content (Thomas, 2004).

Researchers endorse ethics as crucial content for all accounting classrooms (Burton, Johnston, & Wilson, 1991; Griffin & Tyler, 1993; Clikeman & Henning, 2000). Mintz (1995) offers the educator an extensive review of the objectives and theory behind virtue education in accounting, including pedagogical techniques, assessment, and the myriad of challenges related to ethics education. The accounting education literature review of Apostolou, Watson, Hassell, and Webber (2000) offers a range of ethics-related publications, including the purpose of ethical integration in the

classroom, assessment of the ethical standards of students, and various instructional strategies for teaching ethical behavior. Recommendations on methods to address ethical issues include a wide variety of innovative instructional strategies and tools to develop and assess changes in student behavior (Bay & Greenberg, 2001).

Most researchers identify the case study as an effective method of classroom ethics integration (Langenderfer & Rockness, 1989; Gunz & McCutcheon, 1998; Winston, 2000; Baetz & Sharpe, 2004). Scribner and Dillaway (1989) establish the case approach as a superior method to expand classroom instruction and support professional codes. Kiger and Rose (2004) point to student appeal of the case study as a method of enhancing class discussion and student interaction.

Studies point to a need for ethics case studies in tax. A 1988 survey found that client pressures on the tax practitioner to commit fraud were greater than those in the accounting, auditing, and assurance services. Additionally, 50% more litigation occurs in tax than in accounting and auditing (Finn et al., 1988). However, a shortage of classroom cases exists in taxation, particularly those involving ethical issues (Hite & Hasseldine, 2001).

The teaching cases contained herein combine research and ethics in a condensed format that saves both class time and instructor intervention. Students must research the deductibility of education expenses related to acquiring a Masters in Business Administration (MBA), a plausible situation for many future accounting practitioners. Each situation contains unique aspects of a tax practice, including potential issues related to the sustainability of a deduction, use of Internal Revenue Service (IRS) and AICPA ethical guidelines to determine the resolution of the ethical dilemma presented, and client communication.

The overall objective of each case is to develop an understanding of the balance between tax research and ethics, the sustainability of tax positions, and client rapport. An added benefit is the appeal of the topic to the accounting student. The 150-hour rule to sit for the CPA exam generally necessitates an advanced degree; most consider this a prerequisite for success. Resultant student interest in this topic enhances their interest in research and compliance with ethics regulations.

The four scenarios presented replicate realistic situations and provide an opportunity for the student to refine the skills necessary to discern between tax avoidance and tax evasion. Under what circumstances is the MBA deductible? If a practicing CPA or non-CPA decides to return for an MBA or other advanced degree, would the educational costs be allowed? Given the proliferation of court interpretations, how should a tax preparer determine

the likelihood that a certain position will be sustained if examined by the authorities? What specific expenses qualify for the deduction? If the practitioner obtains information from a source other than the client that could affect the deductibility of an expense, can he use the information? How do the ethical guidelines contained in Circular 230 and the Statements on Standards for Tax Practice (SSTP) affect these decisions and guide the practitioner's professional judgment?

Currently, the representative format for the published classroom case includes lengthy narratives and extensive requirements. Recognizing the excessive content and limited time in a college tax course, the design of these cases provides flexibility for the faculty member to select specific learning objectives to suit the individual needs of the class. These case studies can be performed in class or out, at the introductory level or above, in teams or individually, with in-class time requirements ranging from 15 minutes to an hour.

Instructors choose the level of difficulty, the specific facts, the extent of required research, and the overall requirements for submission. Students must analyze the various interpretations of the law, determine the sustainability of client demands for a tax deduction, and establish suitable client communication. Circular 230 and the Statements on Standards for Tax Services (SSTS) provide guidance throughout the process.

STUDENT LEARNING OBJECTIVES INCLUDE

- familiarity with the tax research process;
- interpretation of tax law through an analysis of court cases and administrative rulings;
- determination of the sustainability of a tax position;
- understanding and recognizing ethical dilemmas in taxation;
- decision-making under pressure from outside sources;
- written communication skills application;
- understanding the balance between adherence to the intent of tax law and client retention;
- recognition of the need for interpersonal skills development;
- interpretation of the ethical guidelines associated with tax service providers;
- introduction to the need for enhanced professional judgment to resolve issues in the area of tax services;
- recognizing the professional responsibility to serve both the client's needs and comply with the requirements of the taxing authorities.

CASE STUDY

Expenses for Education: Deduction of Advanced Business Degrees

Background Information for Students

The MBA, popular for decades, symbolizes advanced competencies in business management and commands a starting salary well above that for undergraduates. If qualified, the associated costs, which can range as high as $100,000, are deductible against earned income. Recent court rulings on deductibility present cause for a closer look at the specifics of the law and the interpretation of the courts over time. The cost/benefit of the degree and its affect on lifetime earnings is obvious. Potential tax savings are substantial.

The deduction falls under Internal Revenue Code (IRC) Section 162, which permits ordinary and necessary expenses required to carry on a trade or business, including costs associated with qualifying education. Regulations provide details regarding what does qualify (maintaining or improving skills including meeting requirements for employment retention) and what does not (education that qualifies one for a new trade or business). These generalized requirements, as in all tax law, create the most challenges.

The regulations related to the deduction of the MBA have not been modified since 1967, but litigation in the area occurs frequently due to the high cost of many programs and the possibility of a substantial reduction in taxable income. Examining court and IRS rulings provides critical information for those considering the deduction. As usual, litigation outcomes differ from case to case, depending upon the facts and the courts' interpretation. Generally speaking, the courts and IRS appear to continue their conservative approach when interpreting the specific requirements of education expenses. Taxpayers considering the deduction can determine the sustainability of their position if they have fully researched all the related issues and rulings.

IRC Section 162, as interpreted by Treasury Regulation Section 1.162-5 outlines the requirements for the deductibility of educational expenses. The traditional conservative approach of the tax courts has been to interpret the qualifying deductible education expenses of the MBA as a more profession-oriented degree rather than one of generalized skills. However, the recent tax court case of *Daniel R. Allemeier v. Comm'r* (TC MEMO 2005-07) provides a more liberal interpretation of this regulation, permitting the taxpayer to deduct the tuition costs of his MBA program even though he was advancing on a professional level during the MBA studies (Bates & Waldrup, 2006).

As practitioners, additional consideration must be given to the newly modified ethical guidelines from the IRS and AICPA. All practitioners are subject to the Treasury Department's Circular 230: regulations governing the practice of attorneys, CPAs, enrolled agents, enrolled actuaries, and appraisers before the IRS. Additionally, the AICPA's SSTS replaces the non-enforceable Statement on Responsibilities in Tax Practice (SRTP) and contains in-depth ethical guidance for the AICPA-member practitioner working with any area of tax.

The provisions of these guidelines specify the technical and ethical restrictions on the tax positions a practitioner can take. Tax service providers must interpret these guidelines as they apply to the sustainability of positions taken on a client's tax return. Each case must be interpreted given the facts and circumstances – guided by the reasonable possibility standard based on the likelihood that the position will be sustained if examined by the taxing authorities. The dilemma for the practitioner is how to balance the needs of the taxpayer, who desires a low tax liability, with the requirement of the authorities to comply with the spirit and intent of complex laws and applicable ethical guidelines. The tax service provider's professional judgment is crucial when interpreting and applying the tax law and ethical guidelines.

Situation #1

You are a staff accountant in the tax department of a relatively large regional firm in a major east coast city. Daniel Spears, a client for over 10 years, owns sizeable real estate holdings and other investments. Your firm performs all accounting and tax services for the business. Fees received from Mr. Spears and his related entities represent a sizeable percentage of firm revenues.

Mr. Spears attended a well-known MBA program during the past taxable year. He has indicated that the skills and knowledge obtained will greatly assist his business in the coming years. Costs for attending this program exceeded $20,000. Spears insists upon a current deduction of all related expenses after reading an article in the *Wall Street Journal* touting the benefits of deducting an MBA.

Mr. Spears' current year tax information:

AGI	$ 130,500
Itemized deductions	28,700 (Before qualifying education expenses)

Miscellaneous itemized deduction	1,200 (Before qualifying education expenses)
Marginal tax bracket	28%

Expenses incurred related to education:

Tuition	$20,000
Fees	2,000
Books	700
Meals on campus	820 (*Note*: Some costs are estimated)
Laptop	1,500 (According to the client, purchase for use in the program but also used personally)

Situation #2

Morgan Jackson is an executive at IBM. Her position as vice president of marketing requires a great diversity of skills: communications, marketing, sales, decision-making, demographics, and customer analysis. Her computer science degree, combined with her excellent interpersonal skills, enabled her to move from research into marketing and up the ladder. Ms. Jackson completed graduate work at the state university's executive MBA program, maintaining that the degree was obtained to enhance her skills as an IBM executive.

Ms. Jackson wants to amend her prior year's return to deduct related expenses and expense current year costs in the same way. She had not mentioned the expenditure for the last year as she was unaware of the potential deduction.

The 20-week course ran 10 weeks in the prior year and 10 weeks in the current year. However, you have learned, from a source other than your client, that she is leaving IBM for an executive position at a competitive company. The applicable costs are as follows:

- $64,000 (Per website of program you found the following information: tuition, texts, socials, overnight accommodations, and most meals for the entire 21-month program are included. Friday night residency is required, so the cost of Friday night accommodations and Friday and Saturday breakfast and lunch is included as well as meals and lodging for immersion weeks)

- 960 miles (*Note*: The degree was achieved through weekend classes involving travel from work to school and then returning home at the end of the weekend)

Situation #3

Michael Wessling, a CPA in a small Midwestern town, obtained his undergraduate degree, including hours necessary to sit for the exam, three years ago. Michael has been working for a CPA firm since graduation, but now wants to return to school for an MBA to make him more marketable in the firm and hopefully accelerate his advancement to partner. He currently works in the audit field as a supervisor and is not sure if his expenses will be deductible, although he is aware that certain education expenses are allowed related to graduate degrees. Currently, he has obtained all the necessary coursework needed in accounting, and has obtained the 150 hours necessary for licensing in his state. Since you work in the tax department of the same firm, he has asked your opinion.

Situation #4

William Pierce, CPA, is a 57-year-old controller for a local manufacturing facility. Mr. Pierce has a master's degree in accounting, but wants to obtain an MBA over the next two years. As your client, he confides in you that he wants to teach as an executive in resident at the local liberal arts college when he retires in 6 years. Nonetheless, the MBA will enhance and maintain his current skills. The qualified expenses will total over $18,000 a year for approximately three years. He will take time off work during the day to attend class.

CASE REQUIREMENT OPTIONS

General Questions (Support Each Answer with Appropriate Tax Law from the IRC, Treasury Regulations, Judicial Rulings, and Other Current Sources)

1. What basic requirements exist for allowing the deduction of education expenses related to obtaining an undergraduate degree versus a graduate degree?
2. What specific requirements apply to the deductibility of an advanced business degree?

3. What specific expenses, other than tuition, qualify for the deduction?
4. What specific employment situation must generally exist for the deduction to be allowed?
5. What ethical standards exist to guide tax practitioners in their dealing with gray areas in the law and ethical dilemmas that arise? What do these standards require?

Questions Specific to Scenarios

1. Identify and clarify any concerns that exist in the deductibility of the expenses specific to your client's situation. Draft a memo for the tax file indicating additional information that would be helpful in determining deductibility.
2. What do the AICPA's Statements on Standards for Tax Services (SSTS) and Circular 230 suggest regarding the process of determining the sustainability of a position that appears to be gray? How does this apply to the scenario of your client?
3. Write a letter to the client clearly stating your conclusion on the position. Identify your reasoning, additional information necessary, and any areas of concern.

Teaching Notes

These case studies lend themselves to a variety of instructional strategies with numerous learning outcomes. Each scenario contains reasonable requests for a deduction combined with the requirement that certain gray areas in the law be interpreted. The determination of deductibility allows students to gain confidence in their ability to not only understand, but also interpret tax law while addressing the ethical issues posed by clients desiring a more aggressive position. Requiring students to communicate to the client in writing, particularly when circumstances are challenging, develops and sharpens their written communication skills.

The most beneficial approach requires students to first answer general questions to build a foundation for further research. Students are now ready to move on to specific questions selected by the instructor based on his/her preferred instructional strategy. Students must demonstrate their specific knowledge of the relevant tax law in combination with the SSTS's and Circular 230 by providing persuasive reasoning for their positions and a determination for their position's sustainability should it be examined by the courts.

General guidelines below assist instructors in their assessment of student conclusions. Specific solutions to each scenario are not provided for several reasons. First, the regulations related to the deduction of education expenses date back to 1967. The only current law, therefore, is in the form of tax court cases and a few administrative rulings where case facts and judicial interpretations are inconsistent and rulings are dated.

Second, individual students, depending upon their research findings, will interpret the law differently and faculty must assess the logic and reasonableness of their position. Newly litigated cases related to the deductibility of the MBA appear frequently with a constant change in judicial interpretation. Students must use professional judgment to assess these individual differences.

Finally, a student's determination of deductibility and the possibility of being sustained if examined by the IRS and/or courts also relies heavily upon individual analysis. Applying the guidelines of the SSTS and Circular 230 requires the student to assess the likelihood that the position will be sustained if examined by the taxing authorities. Tax preparers generally may not sign returns that show a position with less than a one-in-three likelihood.

Student solutions may be submitted in a variety of formats:

- Tax research format (Facts/Issue/Law/Analysis/Conclusion/Communication or other comparable layout);
- Case study format;
- In-class discussion;
- Team discussion and class presentation;
- Oral presentation;
- Term paper; and
- Preparation of client letter.

INSTRUCTOR SOLUTIONS GUIDELINE FOR GENERAL QUESTIONS

1. *What basic requirements exist for allowing the deduction of education expenses related to obtaining an undergraduate degree versus a graduate degree?*

   While all income is taxed under Section 61 of the IRC, deductions are allowed only as a matter of legislative grace. The allowance of the deduction for education expenses is included in Section 162 under the

wide-ranging concept of "a deduction of all the ordinary and necessary expenses ... in carrying on any trade or business."

Treasury Regulations (§1.162-5), last revised in 1967, expand, explain, and provide examples related to the specifics of the deduction of education expenses. In general, the following conditions must exist for the expense to be deductible:

- Not required in order to meet the minimum educational requirements for qualification in employment, or other trade or business,
- Not part of a program of study which will lead to qualification for a new trade or business, and
- Maintain or improve skills required by the individual in employment or other trade or business, or
- To meet the express requirements of the individual's employer, or meet the legal requirements to maintain the individual's employment, status or rate of compensation.

2. *What specific requirements apply to the deductibility of an advanced business degree?*

Each scenario's facts and circumstances must be considered but in general the MBA is deductible if the taxpayer is currently employed in a management position and is using the additional education to enhance, maintain, or improve existing skills.

Taken literally, the education expenses must be specifically required, either in writing or by other explicit communication. Does an employer "require" an MBA from an employee? Does the employee assume, that in order to maintain competence, further education is necessary? These questions remain subject to interpretation. As expected, inconsistencies exist with each court and IRS ruling.

3. *What specific expenses, other than tuition, qualify for the deduction?*

- Ordinary and necessary defined by law, litigation, and administration:
  - o standard tuition, fees, and books;
  - o away from tax home: directly related travel, transportation, meals, rent, utilities, and lodging;
  - o costs associated with a management consultant hired for private tutoring;
  - o commuting expenses are nondeductible unless incurred from work to the class where qualifying education expenses occur.
- Pelowski (1985): the taxpayer's costs must be educational versus personal, where the business aspect of the deduction is the primary motivation for incurring these costs [85–1 USTC 9217].

4. *What specific employment situation must generally exist for the deduction to be allowed?*

   Generally, the taxpayer must be engaged in a current trade or business or employment situation. This is where most of the controversy, interpretation and litigation occur with the deductibility of the MBA.

- Education expense allowed if required due to the necessary maintenance or enhancement of the individual's skills.
- Education need only "enhance" existing skills.
- Education obtained should have a "direct and proximate relationship" to the business purpose of the individual's employer.
- Only the minimum education necessary for retention allowed.
- Change in responsibility by the employer does not constitute a new trade or business if the new duties involve the same general type of work.
- Employees are generally considered engaged in a trade or business.
- Section 162 Supreme Court clarification: "the expense must relate to the existing, as opposed to the future, occupation of the taxpayer."
- Revenue Ruling 77-32 – defining an existing trade or business – an anesthesiologist's expenses disallowed related to maintaining his skills during a time when he was not practicing medicine trade or business determination includes continuous and regular activity for income or profit at the time the expenses are incurred.
- Performing service in an employment status does not indicate minimum education requirements have been met.
- Prior to MBA, administrative and management experience is required involving interpersonal and communication skills.
- Courts disallowed MBA deduction for an Army attorney, airline pilot, and quality control foreman.
- Education must meet express requirements of the individual's employer, law, or regulation for retaining an established business relationship, status, or compensation rate.
- Includes customary education for retention or enhancement of competencies for individuals in a comparable profession:
  - o McIlvoy (1979): Courts determined that the reimbursement policy of an employer for the cost of MBA courses taken by an engineer was too lenient and therefore repayments were taxable to recipients as revenue [T.C. Memo. 1979-240].
  - o 1969 Revenue Ruling: Navy Captain allowed to deduct Master of Arts in Personnel Administration: Degree not required by the employer for retention, promotion or salary enhancement, and taxpayer chose to

take the courses which were related to his employment duties [Rev. Ruling 69-199].
  - o McEuen (2004): Deduction denied where taxpayer went from financial analyst firm to industry position that required an MBA [T.C. Summary Opinion 2004-107].
- Expenses disallowed if taxpayer has ability to perform significantly different tasks and activities (new competencies versus the enhancement of existing skills).
- Specialties must be in the same general type of work.
- Law school specifically determined to be nondeductible by the Regulations:
  - o 2002 Galligan case: Law library manager disallowed deduction for a law degree, although she did not practice law – her employer did not require the education [T.C. Memo. 2002-150].
  - o Attorneys disallowed a deduction related to costs incurred to practice law in a new state.
- Greater scrutiny if education expenses appear to provide opportunity for position advancement:
  - o Deduction allowed for teachers obtaining additional education in order to teach in a new school district.
  - o Revenue Ruling 74-78: A dentist practicing general dentistry allowed a deduction for the costs of post-graduate studies in orthodontics.
  - o 2002 Lewis case: Taxpayer disallowed a deduction for expenses related to his MBA undertaken to enhance accounting, financial, and general business skills when he agreed that the degree would qualify him for a "wider variety of positions" [T.C. Summary Opinion 2002-49].
  - o 2003 Zhang case: Individual, assured of employment by a large brokerage firm, was disallowed a deduction for an MBA under the interpretation of a new trade or business [T.C. Summary Opinion 2003-58].
  - o 2005 Allemeier case: Taxpayer attended graduate school part time and was promoted during the time he worked on his degree. The IRS disallowed the deduction, but the courts overruled. [TC Memo 2005-207].
- Occasionally, a temporary leave of absence from work (defined as one year or less) has been allowed as a deductible education expense as long as the taxpayer assumes a similar job in the same employment or trade or business upon return:
  - o Sherman (1977): A two year absence from employment to pursue a graduate degree full time was allowed because he had "suspended

active participation in the field'' while a student and returned after graduation to a similar position [TC Memo 1977–301].

- o Carey (1981): The taxpayer's employer gave him a leave of absence to obtain a post-graduate degree for almost three years. The court indicated that he did not remain in the trade or business. [TC Memo 1981–708].
- o Hitt (1978): A nurse educator attending school to obtain her doctorate was allowed a deduction of her related educational expenses including meals, lodging and travel. The doctorate did not qualify her for another trade or business and the three year period was appropriate for obtaining her degree, which ''sharpened her skills'' as an educator. This case indicated there should be a ''continuing connection to {the} former job {and a} clear indication of an intention to actively carry on the same trade or business upon completion of {related} studies (TC Memo, 1978–1966).''

5. *What ethical standards exist to guide tax practitioners in their dealing with gray areas in the law and ethical dilemmas that arise? What do these standards require?*

The adoption of new AICPA (2000) SSTS emphasizes the unique ethical responsibility of the tax professional to society. Specifically, Preface #1 provides a benchmark for the AICPA-member providing tax services to ensure quality and ethical practices (Holub, 2000). Additionally, all practitioners are subject to the Treasury Department's Circular 230: Regulations Governing the Practice of Attorneys, Certified Public Accountants, Enrolled Agents, Enrolled Actuaries, and Appraisers before the Internal Revenue Service. The provisions of these guidelines specify the technical and ethical restrictions on the tax positions a practitioner can take, providing further pressure for appropriate compliance and interpretation. The IRS imposes censure, reprimand, suspension, or disbarment from practice before the IRS. Penalties from the revenue services exist for frivolous returns, unreasonable tax positions, and intentional disregard for the law (Hammer, 1996).

Statements on Standards for Tax Services

- Standards apply to members of AICPA only
  - o Tax practice and industry.
  - o Tax planning and preparation.

- AICPA Code of Professional Conduct Rule 201: General Standards – guides the SSTS stating that practitioners must
  - o be professionally competent;
  - o properly plan and supervise engagements;
  - o obtain sufficient evidence to support their position; and
  - o exercise due professional care.
- AICPA Code of Professional Conduct Rule 102: Integrity and Objectivity – practitioners must
  - o be unbiased
  - o maintain objectivity and integrity;
  - o be free of conflicts of interest; and
  - o may not knowingly misrepresent facts or subordinate judgment to the client or others.
- AICPA Code of Professional Conduct Rule 501: Acts Discreditable – practitioners may not sign documents containing materially false or misleading information
- Each position should have a realistic possibility of success
  - o Realistic possibility standard: a good-faith belief that the position is warranted by existing law or can be supported by a good-faith argument.
  - o Good-faith belief is based on reasonable interpretations of the law.
  - o The likelihood of audit may not be considered in determining the realistic possibility of success.
  - o AICPA members must determine the realistic possibility by examining relevant facts, appropriate tax authorities, and making a "well-reasoned" conclusion based on reasonable interpretation of the tax law.
  - o Realistic possibility of success is not as strict as the IRC's more-likely-than-not standard.
- All relevant facts should be reviewed for reasonableness
  - o The purpose and substance of transactions should be considered.
  - o Professional judgment must be used to analyze transactions.
  - o Transactions with no economic substance or business purpose must be scrutinized.
- Reasonableness of transactions must be analyzed including
  - o the taxpayer's reputation or experience;
  - o the significance of the advice to the taxpayer; and
  - o the amount involved.
- Members must be advocates for the taxpayer with respect to qualifying positions

Circular 230

- Applicable to all tax preparers.
- Defines tax shelters.
- Requires specific disclosure of potential penalties to accompany any written communication to a taxpayer/client.
- Requires a determination of the reasonable possibility of a tax position being sustained if examined by authorities.
- Disallows tax practitioners from signing a tax return if the realistic possibility standard is not met (a one-in-three chance of being sustained if examined by authorities).
- Tax preparers must determine the reasonableness of the facts given by taxpayer/clients.
- Incomplete information from a tax preparer must be disclosed.
- Tax service providers must acknowledge assumptions in their research.
- Written disclaimers must accompany any written tax advice that contains incomplete advice.

Instructor Solution Guidelines for Questions Specific to Scenarios

1. Identify and clarify any concerns that exist in the deductibility of the expenses specific to your client's situation. Draft a memo for the tax file indicating additional information that would be helpful in determining deductibility.

Situation #1

- Specific details must be obtained concerning campus meals related to whether the taxpayer was out of town when attending school, etc.
- Personal versus educational use of the laptop must be determined.
- Courses should be identified that enhance and improve his existing skills to confirm that the costs incurred do not qualify the taxpayer for a new position.
- How will this affect Mr. Spears' AMT calculations?

Situation #2

- Meals and entertainment may need to be separated, if possible, from total cost of the tuition.
- Mileage from work to school and back may be deductible.
- Ms. Morgan should be thoroughly informed of the details regarding the requirements of the deduction so that she can reveal any potential issues or conflicts related to possible future employment changes.

- Documentation related to her current employment situation would enhance the sustainability of the position in the event of an audit.

Situation #3

- Will the possibility of advancement within an existing position be considered qualification for a new job if the object of staying with a company is to advance?
- Would it be more advantageous for Mr. Wessling to deduct this degree as Continuing Professional Education given the requirement that he can obtain 40 hours per year?
- Has the firm indicated enhanced advancement potential with an MBA?

Situation #4

- Is the desire for a new position in the future considered qualification for a new job if there is uncertainty regarding whether or not the taxpayer will seek this new position?
- Will this degree provide additional enhancement to his current position given that he already has a graduate degree?
- Has Mr. Pierce's employer indicated that the MBA will aid him in his current position?

2. What do the AICPA's SSTS and Circular 230 suggest regarding the process of determining the sustainability of a position that appears to be gray? How does this apply to the scenario of your client?

Professional judgment and a "good-faith belief" of the sustainability of a position appear to be the benchmark terminology contained. However, a pivotal point of these standards is that tax service providers should disclose potential penalties if the position appears to be less than 50% sustainable if examined by the authorities. Additionally, all written communication with the taxpayer must contain a disclaimer if it contains incomplete advice. Students must recognize the subjectivity of professional judgment contained in the ethical standards.

3. Write a letter to the client clearly stating your conclusion on the position. Identify your reasoning, additional information necessary and any areas of concern.

Client letters should contain a restatement of the facts, applicable law including judicial rulings, and a conclusion concerning the rationale of the

recommended tax treatment. Details of the tax law should clarify the conclusion reached. Additionally, according to the ethical guidelines of Circular 230 and the SSTS, appropriate disclaimers should be included. A client letter organized by subtopics would provide clarity for the taxpayer/client. Proper attention to clear, concise writing using appropriate but simple business language and proper mechanics should be a major part of the assignment and related assessment.

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