

1.4: Ethics in Accounting

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Most of those who write about ethics do not make a clear distinction between ethics and morality. The question of what is “right” or “morally correct” or “ethically correct” or “morally desirable” in any situation is variously phrased, but all of the words and phrases are after the same thing: what act is “better” in a moral or ethical sense than some other act? People sometimes speak of morality as something personal but view ethics as having wider social implications. Others see morality as the subject of a field of study, that field being ethics. Ethics would be morality as applied to any number of subjects, including journalistic ethics, business ethics, or the ethics of professionals such as doctors, attorneys, and accountants. We will venture a definition of *ethics*, but for our purposes, *ethics* and *morality* will be used as equivalent terms.

People often speak about the ethics or morality of individuals and also about the morality or ethics of businesses. There are clearly differences in the kind of moral responsibility that we can fairly ascribe to businesses and accountants; we tend to see individuals as having a soul, or at least a conscience, but there is no general agreement that businesses have either. Still, our ordinary use of language does point to something significant: if we say that some businesses are “evil” and others are “corrupt,” then we make moral judgments about the quality of actions undertaken by the business. For example, if we conclude that WorldCom or Enron acted “unethically” in certain respects, then we are making judgments that their collective actions are morally deficient.

Why Should a Business or Accountant Be Ethical?

The usual answer is that good ethics is good business. In the long run, businesses that pay attention to ethics do better; they are viewed more favorably by customers. But this is a difficult claim to measure scientifically, because “the long run” is an indistinct period of time and because there are as yet no generally accepted criteria by which ethical excellence can be measured. In addition, life is still lived in the short run, and there are many occasions when something short of perfect conduct is a lot more *profitable*.

Several accounting organizations have codes of ethics governing the behavior of their members. For instance, both the American Institute of Certified Public Accountants and the Institute of Management Accountants have formulated such codes. It is important to maintain ethical behavior both personally and professionally in business, therefore many business firms have also developed codes of ethics for their employees to follow.

Ethical behavior involves more than merely making sure you are not violating a code of ethics. Most of us sense what is right and wrong. Yet get-rich-quick opportunities can tempt many of us. Almost any day, newspaper headlines reveal public officials and business leaders who did not do the right thing. *Greed* won out over their sense of right and wrong. These individuals followed slogans such as: “Get yours while the getting is good”; “Do unto others before they do unto you”; and “You have done wrong only if you get caught”. More appropriate slogans might be: “If it seems too good to be true, it usually is”; “There are no free lunches”; and the golden rule, “Do unto others as you would have them do unto you”.

An accountant’s most valuable asset is an honest reputation. Those who take the high road of ethical behavior receive praise and honor; they are sought out for their advice and services. They also like themselves and what they represent. Occasionally, accountants do take the low road and suffer the consequences. They sometimes find their names mentioned in *The Wall Street Journal* and news programs in an unfavorable light, and former friends and colleagues look down on them. Some of these individuals are removed from the profession. Fortunately, the accounting profession has many leaders who have taken the high road, gained the respect of friends and colleagues, and become role models for all of us to follow.

Case Study: The Sarbanes-Oxley Act

Sarbanes–Oxley was named after sponsors U.S. Senator Paul Sarbanes and U.S. Representative Michael G. Oxley. As a result of SOX, top management must individually certify the accuracy of financial information. In addition, penalties for fraudulent financial activity are much more severe. Also, SOX increased the oversight role of boards of directors and the independence of the outside auditors who review the accuracy of corporate financial statements.

The bill, which contains eleven sections, was enacted as a reaction to a number of major corporate and accounting scandals, including those affecting Enron, Tyco International, Adelphia, Peregrine Systems, and WorldCom. These scandals cost investors billions of dollars when the share prices of affected companies collapsed and shook public confidence in the US securities markets.

The act contains eleven titles, or sections, ranging from additional corporate board responsibilities to criminal penalties, and requires the Securities and Exchange Commission (SEC) to implement rulings on requirements to comply with the law. “The

mission of the SEC is to protect investors, maintain fair orderly, and efficient markets, and facilitate capital formation.”^[1]

Harvey Pitt, the 26th chairman of the SEC, led the SEC in the adoption of dozens of rules to implement the Sarbanes–Oxley Act. It created a new, quasi-public agency, the Public Company Accounting Oversight Board, or PCAOB, charged with overseeing, regulating, inspecting, and disciplining accounting firms in their roles as auditors of public companies. The act also covers issues such as auditor independence, corporate governance, internal control assessment, and enhanced financial disclosure. The nonprofit arm of Financial Executives International (FEI), Financial Executives Research Foundation (FERF), completed extensive research studies to help support the foundations of the act.

Debate continued as of 2007 over the perceived benefits and costs of SOX. Opponents of the bill have claimed it has reduced America’s international competitive edge against foreign financial service providers because it has introduced an overly complex regulatory environment into US financial markets. A study commissioned by NYC Mayor Michael Bloomberg and US Sen. Charles Schumer cited this as one reason America’s financial sector is losing market share to other financial centers worldwide. Proponents of the measure said that SOX has been a “godsend” for improving the confidence of fund managers and other investors with regard to the veracity of corporate financial statements.

This information about the Sarbanes-Oxley Act was taken from [Wikipedia](#), where you can learn more about it if you are interested.

Important Points to Remember

- **Business ethics** can be described as a set of moral behaviors that influence principles within a business or organizational environment.
- **The Sarbanes-Oxley Act** was created to prevent and limit corporate accounting scandals after Enron financial crimes were revealed in 2001

1. The US Securities and Exchange Commission, <http://www.sec.gov/about/whatwedo.shtml>

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