

**CRIME AND PUNISHMENT IN THE MARKETPLACE:
ACCOUNTANTS AND BUSINESS EXECUTIVES REPEATING HISTORY**

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Abstract: The business world and the accounting profession have experienced several high profile scandals recently, where responsible accountants and other executives could have saved themselves, many investors and others severe personal and financial loss by considering the costs of improper or immoral behavior. This concept is not new. Throughout history, people have taken actions that cost them their freedom, their money and most importantly, their good names. Upon reflection, many of these people are astounded at the seriousness of their action given what little they had to gain from continued involvement. The purpose of this paper is to reinforce lessons that should be learned from cases of business malfeasance. In highlighting many well-known accounting and other scandals, we first develop recurrent themes in the nature of business scandals. We show that many people are responsible for or complicit in the malfeasance.

These individuals could have prevented the fraud or minimized any adverse impact if they had considered their behavior *ex ante*. We show that the employees portrayed demonstrated very low levels of ethical development and seemed to underestimate the probability of getting caught and the resulting punishment. We elicit many reasons from several viewpoints for not becoming involved in fraud. We hope that the next generation of business leaders and middle level staff alike will consider this message when faced with ethical dilemmas. We conclude that the best internal control in a business structure remains the hiring and training of morally upstanding employees and managers who recognize the values of their good names before temptations arise. Incentive plans can encourage ethical behavior. Practitioners must consider fully the potential consequences of their actions no matter how small the perceived probability of a bad outcome.

CRIME AND PUNISHMENT IN THE MARKETPLACE: ACCOUNTANTS AND BUSINESS EXECUTIVES REPEATING HISTORY

“A good name is better than precious ointment,” Ecclesiastes 7:1

As moral agents, we all can choose to act properly or improperly, with resultant rewards or punishments (observable and unobservable). Sadly, from the beginning humankind has too often acted inappropriately to achieve short-term gains, risking their reputations, integrity and “good names.” Three recurrent phases in business malfeasance generally arise. First, one or a few at the top conceive a fraud, often by developing a complex nexus of deceitful activities. Second, audit complacency allows the malfeasance to continue. Last, others—who could stop the malfeasance—comply with requests to carry out the malfeasance or simply allow it to continue. Many involved have very little to gain and much to lose by such improper involvement. In any event, for all involved from top to bottom, upon the uncovering of their actions and inevitable retribution, they realize that the personal and societal cost of the potential gain far outweighed the benefits derived.

Behind the financial problem is a moral problem that has accompanied mankind from the dawn of time. Accountants, auditors, managers and others acting inappropriately risk their jobs, their license to practice, their firm, their freedom and often much, much more. They would most likely realize, albeit too late, that they sacrificed years of training and a good name for little. Besides fears of Earthly punishment, readers holding religious beliefs can also view such behavior as unethical and violating the will of G-d.¹ The following section develops the themes described above in various financial frauds of the last several decades and shows resulting economic losses. We show that models of ethics forbid such malfeasance. In the last section, we

¹ We do not spell out the divine name since many religions view it as improper unless it is part of a prayer service.

show that mainstream religions forbid such malfeasance with dire consequences for the sinner. We then present our conclusions.

[PLEASE INSERT TABLE 1 HERE]

The following relatively higher profile cases from various eras and cultures illustrate the decisions that fraud perpetrators and others complicit in frauds often make, which otherwise are reflective of other observed fraud cases. Clear themes emerge when studying them in tandem.

Case 1: Equity Funding Corporation of America

Equity Funding Corporation (Equity) [1978] had an intriguing financial concept: offer mutual funds to customers and service customer life insurance policies with mutual fund profits. At the end of the required payment terms on the life insurance policies, investors could redeem their mutual fund shares or cash values from their paid up life insurance policies to repay any of their mutual fund loans. The investors then kept appreciation of the investment in excess of amounts paid on the insurance loans. This type of leveraging is perfectly legitimate, albeit risky.

In the mid-1960s, Equity's Chair and CEO, Stanley Goldblum, sought to acquire other companies. Because he used Equity stock to complete the acquisitions, he needed its stock price to remain strong. When its earnings fell short of those of the prior year, he ordered the recording of fictitious commissions to help achieve earnings growth targets. Soon, Equity began to issue fictitious policies and then sell them to reinsurance companies for cash; it then originated and sold other fictitious policies to help pay subsequent premiums to the reinsurance partners. It even reported deaths on past fake policies to collect on the reinsurance firms' death benefits.

This scam lasted for several years, involving many employees. A computer programmer even generated a program to produce fake policies, and teams of employees often scrambled to document bogus policies when auditors requested policy detail files. A participant in this matter

commented, “It takes a long time and you have to be careful about date stamps and other details. But I had fun being the doctor and giving the guy’s blood pressure and all that” (Hancox, 1997). Obviously, Goldblum was in the best position to stop this malfeasance. Many of the employees who participated in this scam in order to maintain continuing employment in reasonably well-paid jobs could well have taken their talents to other, more honest entities, likely at comparable salaries. However, they didn’t and they paid a large price as Goldblum and 18 other conspirators ultimately pled guilty to participating in the fraud, and investors lost hundreds of millions of dollars. Those involved should have realized that no potential gain from such fraud could adequately offset the potential price of their bad behavior, despite probably knowing that they could not continue this scheme for long, as they would need to develop ever-increasing amounts of bogus policies. The additional costs are a matter of one’s personal beliefs.²

Case 2: ESM Government Securities

ESM Government Securities (SEC, 1985) bought and sold federal government debt securities for resale to moderate-sized banks and municipalities for “repo” and “reverse-repo” (financial hedging and window-dressing) purposes (e.g., to minimize potential risks and to improve their financial statements’ appearance). Its auditors, Grant Thornton [GT], knew of the potential risks of ESM simultaneously selling such securities to more than one customer, especially when customers did not take physical possession of the purchased debt instruments.

Soon after ESM lead auditor Jose Gomez became a GT partner in 1987, Alan Novick, a high-level ESM executive, told him that ESM had committed illegal acts and falsified its financial statements. Novick stressed that if Gomez disclosed the schemes, AG would lose a major account, but Gomez might lose his new position. He asked Gomez to work with him to help clean up these problems for everyone’s benefit. Gomez accepted this arrangement and

² For additional details, see Messier, Glover and Prawitt (2005), Seidler et al. (1974), and AICPA (1975).

received about \$200,000 from ESM officials, which led to his receiving a 12-year prison term (he served four and a half years). AG paid \$175 million in civil court settlements, and ESM was dissolved. Despite Gomez's possible good intentions, his continuing involvement in this wrongdoing impugned his and AG's good reputation and led to significant financial losses for all those associated with ESM.³

Case 3: CUC International (Cendant)

E. Kirk Shelton, Walter Forbes and Cosmo Corigliano (this last Chief Financial Officer (CFO) of CUC International, which ultimately became Cendant Corporation) were prosecuted for their parts in a massive accounting scandal. Corigliano testified that in 1995 he was promised an \$80,000 bonus if Cendant earnings reports met specified target levels, leading him to work closely with Forbes and Shelton to continually misstate financial reports to meet earnings targets. Cendant used schemes such as not reversing revenues related to unrealized membership payments that credit card companies rejected and recording membership payments as revenue currently rather than over the appropriate annual periods. In all, Cendant reported tens of millions of dollars in fraudulent revenues "to hit the number the financial community was expecting" (*Bloomberg News*, 2004). Corigliano made about \$170,000 per year in salary, plus an \$80,000 bonus. Given his experience level, he could well have gotten a job at another company for at least \$100,000. Thus, for \$150,000 or less, he participated in the fraud. In 2000, he pled guilty to criminal fraud charges and is now serving a five-year prison sentence. In 2004, he agreed to pay \$14 million to settle regulatory charges related to the fraud (Milford 2002).⁴

³ For additional details, see Messier, Glover and Prawitt (2005).

⁴ For additional details, see Milford (2002).

Case 4: HIH Insurance

Australian accounting rules require financial statements to provide a true and fair view of the company, which the financial statements of HIH Insurance Group, a large Australian insurance concern, did not provide before its collapse. The \$5 billion (Australian) misstatement was very straightforward--grossly understating reserves for future claims, thus grossly overstating its net assets (Commonwealth of Australia, 2003). Ultimately, HIH could not pay for the incurred claims and became insolvent. HIH had entered into other dubious transactions and business relationships, which further drained company cash. Thus, capital providers lost their investments and insured customers were left without warranted claims payments. The losses eventually exceeded \$5 billion (Australian).

HIH's dominant personality was long-time CEO Raymond Williams, who, with Michael Payne, founded the business in 1968. Williams oversaw several transactions and business arrangements fraught with risk, as well as grossly misleading financial reports. For example, at December 31, 2000, HIH fraudulently reported a reserve for future claims totaling \$3.1 billion, which an independent actuary later estimated should have been at least \$5 billion, or more than 60% higher.⁵ Williams could not have believed that the financial statements were a true and fair depiction of the company's financial condition. As a long-time principal with HIH, he risked a sizeable investment and salary, which likely totaled millions of dollars. Of course, Williams ultimately lost these fortunes as well as his good name. While the complicity of complacent auditors and internal HIH personnel is not as well documented in this case, it is almost certainly present in a company of this size and a case that is so simple in nature.

⁵ For additional details, see Commonwealth of Australia (2003).

Case 5: Enron

Just before its famous collapse, Enron had an \$80 billion market capitalization as one of the world's most admired companies. Today, it is bankrupt, with its investors and employees losing billions of dollars. Enron's collapse arose from bad investments, over-leveraging and the revelation of huge obligations that were inadequately reported in its financial statements. Like the other cases, Enron involved a nexus of activities designed to confuse.⁶ Key internal figures in this debacle include Chair and former CEO Ken Lay, President Jeffery Skilling, CFO Andrew Fastow, Chief Accounting Officer (CAO) Richard Causey, Chief Risk Officer Richard Buy and Assistant to the CFO Michael Kopper. They and other mid-level accountants could have stopped this malfeasance before well before billions were lost. Also complicit were Arthur Andersen and lead Partner David Duncan, whose partners debated dropping Enron as a client a few months before the collapse. Ultimately, the firm retained this client, noting that it was then the firm's second biggest client and could soon become its largest and produce revenues as high as \$100 million, including large amounts for non-audit services (*Guardian Newspapers*, 2001). Duncan earned \$700,000 annually to manage this account, plus part of Andersen's partnership profit pool. To appease Enron, he apparently did not require many large audit adjustments for several years, and often signed off on financial statements that were, by any reasonable standards, unclear and misleading (Fisher, 2002). This shoddy work and attempts to eliminate key evidence led to Andersen's felony conviction and demise—apparently ignoring its founder's key slogan of “think straight and talk straight.”

⁶ For additional details see Raghavan et al. (2002), Emshwiller (2002), Weil et al. (2001), Kranhold et al. (2002), Seligman (2002), Wee (2001) and Zellner et al. (2001).

Case 6: WorldCom

WorldCom's accounting scandal involves many people including CEO Bernard Ebbers, CFO Scott Sullivan, CAO David Myers, Accounting Director Buford Yates, and accountants Troy Norman and Betty Vinson. The accounting misstatement was simple. WorldCom often capitalized (rather than expensed) costs paid to lease communications line capacity from local phone networks, which benefited only current periods. Such improper procedures allowed it to delay expenses and, more importantly, to report the costs as investing outflows on the Statement of Cash Flows, which grossly overstated two key performance measures: operating cash flows and earnings before interest, taxes, depreciation and amortization (EBITDA). It also conspired to misstate the reserve for uncollectible accounts and used that reserve to manage earnings. Its bankruptcy cost its investors and creditors billions of dollars, and its employees their jobs.⁷

Ebbers and Sullivan often asked its accountants, Myers, Yates, Norman and Vinson to misstate accounts. Risking only their salaries (plus Myers' and Yates' bonuses) by this complicity, they remained with WorldCom, as they became increasingly troubled. Given the relatively low unemployment rate at the time of the fraud and given the quality of their experience as corporate accountants, they most likely could have gone elsewhere for much of their WorldCom salaries. Ultimately, these accountants reported the problems to the SEC. In any event, Ebbers was recently found guilty of fraud and sentenced to 25 years in prison.

Case 7: Parmalat

Parmalat, Italy's largest dairy company, remains under investigation as authorities seek to unravel a web of fraudulent transactions and shell companies used to cover financial losses and raise capital. Details of this fraud continue to emerge as the investigation proceeds. The fraud became public when Bank of America revealed that a \$4 billion US deposit that Parmalat

⁷ For additional details, see Gross (2002).

reported did not exist. This deposit was among the assets that Bonlat, a Parmalat subsidiary (based in the Cayman Islands) reported. The fraud will harm Italian dairy farmers, who are due a collective 120 million euros, and world-wide equity and debt investors who stand to lose billions.

Parmalat's CEO Calisto Tanzi and others were arrested for "promoting, directing and organising the operation (*BBC News* 2003)," as were company accountants accused of issuing false information about its finances, hiding losses and debt in special purpose entities under company control, and fabricating assets and deposits as a basis to raise capital. Its independent auditors, Grant Thornton, were also arrested, accused of "suggesting ways for the company to commit fraud" (*Guardian Newspapers*, 2003). Grant Thornton's and Parmalat's lower management level accountants' involvement is especially puzzling since they face large civil and criminal penalties and seem to have had relatively little to gain except their respective shares of Parmalat profits, some human capital, their continuing salary and potential bonuses.

Case 8: Adelfia Communications

John J. Rigas, founder and CEO of cable television company Adelfia Communications bought a small cable franchise for \$300, which grew remarkably, mostly through aggressively acquiring existing companies. Ultimately, he took Adelfia public, garnering many millions in the initial public offering of his shares. In 2002, Rigas and his son Timothy were arrested for seeking to defraud its shareholders. Both were convicted in 2004 and face up to 30 years in Federal prison. The Rigas took money from Adelfia to finance their extravagant personal lives, the costs of which prosecutors estimated to exceed \$100 million. The investor deceptions involved making unreported liabilities totaling over \$2 billion that they shifted to unreported affiliate subsidiaries and overstated statistics about their growth of cable customers (SEC 2002).

While the amounts of this fraud may seem large, the Rigas didn't need the money because they made millions when Adelphia went public. The family lived a famously extravagant lifestyle including owning luxurious homes across North America, and a personal jet and golf course. To finance their lifestyle, the family treated Adelphia like a personal bank account and covered up the activity by producing misleading financial reporting. John Rigas is 79 years old. He was in his 70's when the worst of the company looting occurred. These actions will almost certainly cause him to spend the rest of his life in prison. Again, while the roles of lower level employees are not as widely documented in this case, they are almost certainly present given the size and complexity of Adelphia.

Case 9: Alfred Taubman (Sotheby's)

Alfred Taubman once had had an excellent reputation as President of a massive shopping center enterprise. *Forbes* magazine estimated his wealth at over \$600 million, and he gave millions of dollars to many charities. He also served as Chair and majority owner of Sotheby's auction house. Despite this wealth, he served a year in prison, was fined \$7.5 million and paid out \$186 million to plaintiffs in civil lawsuits for conspiring to fix commissions from sellers of fine art (Dixon, 2002). From 1993 to 1999, Taubman and executives from competing auction houses conspired to inflate selling prices on certain high value art and to set inflated commission rates in the industry, exempting only a small, agreed-upon list of preferred customers from such high commissions. Prosecutors estimated that Sotheby's and rival Christie's auction houses netted about \$44 million in additional commissions as a result of the scheme, but spent about \$500 million in fines and settlement. Taubman probably later realized that he sacrificed his very good name for a very small portion of his vast wealth.

In upcoming sections, we summarize the ethics and moral reasoning literature and the religious literature. These literatures are related but not redundant. The literature in ethics describes a linear hierarchy of ethical reasoning levels that individuals climb (or fail to climb). The world's major religions hold their followers to the highest ethical standard, which should make many of its followers seek to ascend to the higher levels of moral reasoning.

Ethics and Business Fraud

The academic literature has sought to understand managerial reasoning processes that will explain ethical breakdowns in business. The theoretical underpinning of moral reasoning research is drawn from Kohlberg's (1969, 1973, 1981, 1984) theory of moral development, where individuals proceed through a sequence of six distinct stages of moral reasoning ranging from adhering to rules because of fear of punishment to adhering to rules due to concern with ethical principles and respect for the dignity of humans. His model entails three levels of moral development: the "preconventional," "conventional" and "post conventional" levels. In the preconventional level, individuals use egoistic or self-interest concepts to solve moral problems. The basis for morality in Kohlberg's first stage of the preconventional level is punishment for disobedience. In the second stage of moral development of the preconventional level, individuals reason what they stand to gain from the behavior. The conventional level of moral development is a utilitarian level, where individuals consider society's expectations and overall welfare. The conventional contains two stages of development: stages three and four. Stage three is the "Good Boy/Nice Girl" orientation, where the basis for morality entails others viewing individuals favorably. In stage four, the "Law and Order Orientation," individuals conform to societal norms to promote order and overall societal welfare. Next, in the highly principled post conventional level, individuals use universally accepted concepts of rights and

justice to resolve moral dilemmas. The fifth and sixth stages of development comprise the post conventional level. In stage five, individuals adhere to that society's highest standard. In stage six, individuals adhere to high ethical principles without regard for particular societal norms.

Many studies have criticized, expanded upon and applied Kohlberg's theories to the general population and to accountants. Rest (1979) and Trevino (1986) argue that moral reasoning is a valid means to operationalize the decision-making processes used to solve moral problems. Gilligan (1982; 1987) posits that Kohlberg's work fails to consider certain gender issues of morality. Rest (1979; 1990) developed the Defining Issues Test (DIT), which asks the subjects to make decisions about social dilemmas (e.g., if a relatively poor individual should steal medicine for a dying spouse) to derive a Principled (*P*) score that measure their concern for others or belief in basic fundamental and self-determined values.

These DIT scores relate to subjects' moral reasoning ability (MRA) under Kohlberg's framework (Clarke et al., 1996), which forms the bases for many studies on accountants' perceived MRA. For example, Ponemon and Gabhart (1993) found that US accountants generally have lower MRA scores than expected, given their age, education and experience, and that Canadian Chartered Accountants have higher MRAs than equivalent U.S. CPAs. Using scales similar to Rest, Kracher et al. (2002) found that (1) Indian business professionals had significantly higher MRA than did Indian students and U.S. business professionals currently in graduate schools; (2) Indian professionals significantly lack trust in their industries; and (3) education significantly affects MRA scores. Elias (2002) found that accountants with high (low) perception of social responsibility viewed earnings management actions as more unethical (ethical), and idealism and relativism relate significantly to earnings management ethics. The results also indicate a strong positive relationship between perceptions of corporate ethical values

and earnings management ethics. Organizational accountants in different occupations with high (low) ethical values perceive earnings management actions as more unethical (ethical).

Kohlberg found that most individuals never move beyond the law and order stage, and the culprits mentioned in the above cases never rose beyond the conventional level. Absent intervention, most adults continue to reason about moral dilemmas at the conventional level. Blasi (1980), Rest (1979), Weber (1990) and others found that since moral reasoning correlates positively with education level and with age, older adults and more educated individuals will more likely rise to higher levels of moral reasoning. While organizational codes of conduct can effectively help communicate management's ethical expectations to employees, mixed evidence exists as to whether adult ethics training enhances ethical behavior and decision-making.

Snyder (1974), Snyder and Cantor (1979) and Snyder and Gangestad (1986) described individuals' self-monitoring characteristics. A low self-monitoring individual looks internally to determine the appropriate behavior in a given situation. A high self-monitoring individual is more likely to alter his/her behavior to fit the norms of a given situation. Hence, a high self-monitoring individual is more likely than a low self-monitoring individual to be affected by the culture of an organization. As a result, low self-monitoring individuals are more likely than high self-monitoring individuals to achieve a post-conventional level of moral reasoning.

The climate in the organization might also impact an individual's behavior. The organization's climate is the "shared set of norms, values and practices of organizational members regarding appropriate behavior in the workplace" (Elm and Nichols 1993, p.820). Past studies have used individuals' perceptions of the ethical climate as a measure of the ethical climate or the organization (e.g., Glick 1988, Victor and Cullen 1987, 1988).

Characteristics of the moral issue itself are also relevant. Ferrell and Gresham (1985) demonstrated this by noting that undoubtedly fewer people would endorse embezzling company funds than would endorse padding an expense account.

The accounting literature contains some findings about the accountants' moral reasoning. Gaa (1995) synthesizes these findings as follows: "(1) the degree of moral development of accountants resembles the general population more than it does groups with comparable education and occupational status; (2) occupational choice and type of education may influence the moral development of members of the profession; (3) organizational factors are reflected in the relationship between subjects' rank in the organization and their degree of moral development; (4) females have higher moral development than males; and (5) accountants of different nationalities have different degrees of moral development."

[PLEASE INSERT TABLE 2 HERE]

Widely accepted ethical systems combine the various incentives to behave ethically. Some are more secular. Others are religion-based. Regardless, one must have reached at least Kohlberg's "conventional level" to act ethically under any of the ethical systems, and certainly all forbid the actions outlined in the earlier cases.⁸

[PLEASE INSERT TABLE 3 HERE]

Ethical Relativism: "No principles are universally valid. All moral principles are valid relative to current tastes. The rules of the society serve as a standard." (See footnote 8) While this is arguably the weakest of the ethical systems, it certainly condemns fraud since our society forbids and punishes fraudulent behavior and/or complicity in such activities.

⁸ Further details on ethical systems, including the section below, appear in ethics textbooks or websites such as www.accessexcellence.org/AE/AEPC/WWC/1992/ethical_systems.html. This website provided these summaries.

Divine Command Theory: “Moral standards depend on G-d who is all-knowing. Any act that conforms to the law of G-d is right; an act that breaks G-d’s law is wrong.”⁸ Despite periodic moral and even physical battles among these great religions, Christianity, Judaism and Islam all condemn business malfeasance. The authors of this paper are partial to this theory as we adhere to these principles and believe that the potential cost for such activities greatly exceeds any potential Earthly gain.

Utilitarianism: “Actions are judged right or wrong solely by their consequences. Right actions are those that produce the greatest balance of happiness over unhappiness. Each person’s happiness is equally important.”⁸ While Utilitarian thinking can be problematic, it certainly condemns business malfeasance since only a very few stand to gain while many lose.

Deontology: “Emphasis is on moral rules and duty. If not willing for everyone to follow the rule, then it is not morally permissible, emphasizing autonomy, justice and kind acts. People treated as ends, never means.”⁸ Again, this ethical system prohibits fraud and supports harsh punishment for the fraudulent.

Virtue Ethics: “Morals are internal. It seeks to produce good people who act well out of spontaneous goodness. It emphasizes living well and achieving excellence.”⁸ This ethical system condemns business malfeasance by encouraging all citizens’ virtuous behavior.

The accountants and business professionals portrayed in the earlier cases were clearly operating at very low levels of moral development. Further, all of the widely accepted ethical systems clearly forbid the behavior. Unfortunately, such malfeasance has occurred since biblical times. In the next section, we provide examples and lessons from the Old Testament, the New Testament and the Koran of similar activities and the resulting price paid. We hope that these

will serve to remind the billions of followers of these religions of these principles to help them to resist future temptation to become involved in fraud.

Religion and Business Fraud

Millions of people worldwide who follow faithfully mainstream religions will likely look to their religion to provide moral direction. Certainly, all mainstream religions forbid complicity in malfeasance and promise dire consequences for the sinner. The following discussion indicates some key lessons from Judeo-Christian and Islamic orthodoxy to reinforce this point.

[PLEASE INSERT TABLE 3 HERE]

Jewish law often states the importance of keeping a good name (e.g., Adam and Eve, Esau, Joseph's brothers, Korah and Achan). Leviticus 25:6-7 considers all produce of the (seventh) Sabbatical year as "ownerless" and free for everyone to take, banning its use for commercial purposes. The Talmud (Kiddushin 20a, Sukkah 40b) warns that those seeking money by doing business with produce of the Sabbatical year, "will lose all their chattel and fields, until they are forced to sell their homes and themselves [into slavery]." Similarly, the Be'er Hagolah, Commentary on the Code of Jewish Law, prohibits Jews from seeking wealth by deceiving gentiles. The smallest theft or swindle demonstrates a substantial lack of faith in G-d, which vastly diminishes any perceived ill-gotten gain. Such ideals imply that people should want to act properly, if only to retain their good names. Custodians of stakeholder-provided money in business should also act properly. This focus on proper conduct resembles the ideal from the opening part of the American Institute of CPA's Code of Professional Conduct, which quotes Marcus Aurelius, "A man should be upright, not kept upright."

The New Testament also draws upon many Old Testament characters and lessons. Combining the impact of money and greed on judgment, Jesus said, "It is easier for a camel to go

through the eye of a needle than for a rich man to enter the kingdom of G-d” (Matthew 19:24). Paul added that “people who want to get rich fall into temptation and a trap and into many foolish and harmful desires that plunge men into ruin and destruction” (1Timothy 6:9). Thus, wealthy people, who often face many moral issues, should especially guard their good names.

Similarly, in Sura 104 (Humaza the scandal-monger) of the Koran, those thinking that their wealth will last forever face G-d’s wrath if they obtained such wealth immorally. Moreover, if they attack the character of their adversaries—even if true—in order to gain worldly goods, their efforts will lead to naught, or possibly worse, in the next world.

CONCLUSION

The above examples show that many people from many countries gave up their good names and more, even knowing they were doing wrong and often realizing the relatively puny benefits of the actions. They grossly underestimated the probability of getting caught, the total cost of getting caught, or both. Only upon getting caught did they fully reflect upon the actual cost of their action both in dollars and in damage to themselves as well as to their families, friends and colleagues. In these examples, some individuals temporarily gained riches while others gained little. Some designed selfish schemes to steal and defraud. Others simply didn’t stop the activities or played a small part by remaining silent. All have some culpability. The consistent theme is realizing ex post that the activity was not worthwhile.

Carson (2003) shows that, in light of the Enron, WorldCom and other recent scandals, many companies engage in such perverse ethics policies as short-term stock option incentives that help create corporate cultures that promote unethical financial reporting and having top managers encourage their subordinates to act unethically. Several behavioral and economic theories can help explain such irrational phenomena as employees acting dysfunctionally in times

of stress and heightened risk. Kahneman and Tversky's (1984) prospect theory shows that under times of heightened risk and uncertainty employees often overvalue large (often adverse) probabilities and undervalue larger probabilities. Similarly, Bowman (1982) finds that many troubled firms prefer and seek risk. For example, Levi Strauss & Co. bases one third of an employee's evaluation on aspirational behaviors including value diversity and ethical management, and HCFA rewards physicians for not placing the company at risk (e.g., not performing unneeded tests for their patients).

Whether we are economic engines, moral persons or religious beings, when considering such actions, we should step back, consider *both* the potential rewards and consequences of our actions and resist. Tempted persons should focus on the value of their good names, remembering those who lost this most precious asset. From the company's perspective, a key aspect of internal control is diligently searching for employees that display moral development at the post-conventional level. Finally, companies should avoid furnishing incentives for dysfunctional short-term managerial focus.

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TABLE 1**EXAMPLES OF BUSINESS LEADERS AND CPAs “SELLING OUT”**

	Moral Agent - Recent	Agent’s Potential Gain	Action taken by Agent	Result of Agent’s Action
Case 1	Stanley Goldblum and other key Equity Funding executives/employees	Goldblum sought some wealth and the employees sought to maintain their salaries and company positions.	Employees fabricated insurance policies to collect commissions and death claim payments from reinsurers.	18 employees and Goldblum pled guilty, and investors lost millions of dollars.
Case 2	Gomez, lead ESM Auditor for Grant Thornton	\$200,000 and remain as a Grant Thornton Partner.	He let ESM continue issuing fraudulent financial statements for several years.	Gomez served 4.5 years in prison; the firm made civil payments totaling about \$175 million.
Case 3	Cosmo Corigliano, Cendant Employee	\$80,000 bonus.	Corigliano manipulated records to misstate financial results and meet earnings targets.	He faces 10 years in prison for criminal fraud and has paid \$14 million in fines.
Case 4	Raymond Williams, CEO of HIH Insurance Group	HIH holdings and salary.	Williams orchestrated financial statement misstatements that misled investors.	Williams lost his fortune and investors lost about \$5 billion (Australian).
Case 5	David Duncan, Andersen partner for Enron	Total professional fees of about \$52 million; salary of \$700,000 for Duncan.	Duncan improperly oversaw the Enron audit; Andersen destroyed key documents.	Ultimate dissolution of Arthur Andersen.
Case 6	Four of WorldCom’s internal accountants	Desire to keep a current job/salary.	They obeyed executives’ orders to misstate earnings, but later reported events to the SEC.	They face 10 - 15 years in prison and may no longer be officers of public companies.
Case 7	Parmalat’s CEO Tanzi; its accountants and auditors	Tanzi desired to maintain profitability, auditors wanted to keep the client.	Conspirators issued false investor information; auditors are accused of aiding the fraud.	Bankruptcy, whose ultimate penalty to those involved is yet undetermined.
Case 8	John and Timothy Rigas, Adelphia Communication	Approximately \$100 million for a family that already had extraordinary wealth.	Paid personal expenses from company funds, which they masked by fraudulent reports.	John Rigas will almost certainly spend the rest of his life in Federal prison.
Case 9	Alfred Taubman, co-owner of Sotheby’s	Incremental profits on auctioned items.	Taubman orchestrated a price fixing scheme with executives at Christie’s	He spent a year in prison, fined \$7.5 million and paid \$186 million for civil lawsuits.

TABLE 2

KOHLBERG'S STAGES OF MORAL DEVELOPMENT

LEVEL / STAGE

LEVEL: Preconventional

Stage 1: Punishment and Obedience Orientation

KOHLBERG'S SIX STAGES OF ETHICAL REASONING

Stage

What is right?

Reasons for doing it

Pre-conventional level — focus on self

Stage 1

Avoid breaking rules backed by punishment; Avoidance of punishment or harm to self

Stage 2

Follow rules if they are in own interest; To serve one's own immediate interest

Conventional level — focus on the group

Stage 3

Living up to what is expected by people; Need to be a good person in the eyes of others

Stage 4

Fulfilling agreed-to duties and obligations; To keep the social institutions going

Post-conventional level — focus on inner self

Stage 5

Upholding non-relative obligations first; Obligation to law before social contracts

Stage 6

Follow self-chosen ethical principles; Belief in ideal as a rational person

TABLE 3
ETHICAL SYSTEMS

DESCRIPTION	STRENGTH/WEAKNESS	EXAMPLE
ETHICAL RELATIVISM – Using society’s rules as a standard, no principles are universally valid. All moral principles are valid relative to cultural tastes.	S- Brings about tolerance of other cultures. Keeps societies from falling apart. W- Confuses what ought to be done with what is currently done.	South Seas Islanders practice cannibalism. Cannibalism is strictly prohibited in the U.S.
DIVINE COMMAND THEORY - Moral standards depend on an all-knowing G-d. Acts conforming to the law of G-d are right; acts that break G-d's law are wrong.	S- Standards are from a higher authority than humans. Gives reasons why man should behave morally. Gives worth to all equally. W- Depending on interpretation, can be arbitrary. Can we know true divine authority?	Christian religions point believers to rules like the Ten Commandments.
UTILITARIANISM - Actions are judged right or wrong solely by their consequences. Right actions produce the greatest balance of happiness over unhappiness. Each person's happiness is equally important.	S- Promotes human well-being and attempts to lessen human suffering. W- One person's good can be another's evil. Hard to predict accurately all consequences.	The U.S. dropped the atomic bomb on Japan in WWII believing it was worth the loss of life to gain the end of the war and stop the higher loss of life if the war continued.
DEONTOLOGY - Emphasis is on moral rules and duty. If not willing for everyone to follow the rule, then it is not morally permissible. Emphasis on autonomy, justice and kind acts. People treated as ends, never means.	S- It provides a special moral status for humans. Moral rules are universal. W- It says nothing about other living things. Rules can be abstract.	In the U.S. a continued emphasis on human rights for all people stems from a willingness to reason that justice and equal treatment ought to be applied universally.
VIRTUE ETHICS - Morals are internal, seeking to produce good people who act well out of spontaneous goodness. It emphasizes living well and achieving excellence.	S- It internalizes moral behavior. W- Offers no guidance for resolving ethical dilemmas.	A faculty determines that a student council officer with a genuine interest to serve deserves more recognition than one who just wants to beef up his resume

Note: This table is excerpted from Introduction to Types of Ethical Systems. This paper presents an introduction to classic ethical systems. For additional details see http://www.accessexcellence.org/AE/AEPC/WWC/1992/ethical_systems.html