

# Ethical Dilemmas in Management Accounting: A Study of Ethical Judgment and Ethical Intentions to Act.

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## Introduction

Management accounting (hereafter MA) involves internal corporate accountants who provide information, advice and reports to assist management in making informed business decisions. Despite the importance of the MA process, there is surprisingly little empirical evidence of the ethical judgment and intentions to act ethically when engaging in the complex interactions and transactions that are associated with the MA function. Additionally, we are unaware of any research that has investigated whether or not the new ethics requirements at most business schools has had any effect on ethical recognition, judgment or intentions to act ethically.

To better understand key MA-related ethical dilemmas that often arise in practice, the present study addresses two fundamental ethical issues in MA by employing ethics-related vignettes that relate to expense reclassification strategies made under stress. Specifically, the vignettes include an operational expense reclassification to an asset in order to avoid debt covenant noncompliance and expense reclassification from a proposed capital budgeting project to normal operations in order to increase projected internal rates of return (IRR), and

thus enhance the chances of receiving project funding.

This research is important because it will inform researchers of the likely responses managers will employ when they face such real-world ethical dilemmas and stressors. Survey questions probe respondents' perceptions relating to ethical issue recognition, ethical judgment, and ethical intentions, as well as moral intensity and perceived importance of an ethical issue (PIE), ethical orientation (e.g. deontological), Big Five personality traits, and ethical training in college, among other independent variables and demographics.

## Background

Extant MA literature documents specific organizational benefits of setting work performance goals, including greater effort and persistence by subordinates who are faced with challenging performance benchmarks (e.g., Locke and Latham 1990; Luft and Shields 2003). More generally, the MA goals literature provides a foundation to examine whether working to meet specific, difficult goals increases performance across a broad range of cognitive and physical tasks. This relationship is strong enough that goal setting is a central element of motivation theory and management education (Ambrose and Kulik 1999).

However, a common cause of dysfunctional behavior in organizations is the use of financial goals (meeting budget targets, for example) as criteria for performance evaluation (Hope and Fraser 1997, 2000, 2003; Jensen 2001, 2003). In particular, the use of goals to set subordinate compensation levels may encourage employees to engage in undesirable behaviors in order to improve the likelihood of achieving targets (e.g., Jennergren 1980; Healy 1985; Young 1985; Chow et al. 1988; Kohn 1993; Pfeffer 1998; Schweitzer et al. 2004; McNabb and Whitfield 2007; Ordóñez et al. 2009).

Three specific areas of potentially unethical behavior in MA include setting a target below what the actor believes is achievable (budgetary slack), misrepresentation of performance (falsified reporting), and inappropriate conduct (workplace ethical issues). Budgetary slack may be unethical if it leads to misallocated resources, suboptimal firm performance, and lower return on investment (Lukka 1988; Degeorge et al. 1999; Douglas and Wier 2000; Jensen 2003). The predominance of accounting ethics studies assessing budget-related issues focus on budgetary slack (e.g., Chow et al. 1988; Davis et al. 2006).

In the second case, goal setting may motivate individuals to misrepresent their performance levels. For example, employees at Bausch and Lomb during the 1990s, under pressure to reach sales targets and earnings goals, reported sales that never took place resulting in falsified financial statements (Plunkett and Rouse 1998). More recently, employees at Wells Fargo created over a million phony accounts to improve performance measures – an action that resulted in over 5,000 employees losing their jobs and fines of \$185 million when the scandal came to light (Egan 2016).

Finally, individuals may engage in unethical actions and methods to achieve their goals. Actions toward customers, such as aggressive behavior or attempting to sell unnecessary services to customers for the purposes of increasing performance evaluations, pecuniary rewards, or organizational status are also unethical (Burns and Kiecker 1995; Pfeffer 1998; Douglas and Wier 2000; Jensen 2003).

Based on the above literature review, there is a paucity of research devoted to the misrepresentation of performance, including falsified performance. The present study attempts to address this gap in the literature. The base scenarios address misrepresentation of

performance issues. For example, in Scenario 1, the moral agent decides to capitalize repairs that should be journalized as revenue expenditures under generally accepted accounting principles (GAAP). In scenarios 2 and 3, the moral agent reclassifies expenses from an internal capital budgeting project to normal operations in order to falsely inflate project IRR.

This study should significantly contribute to the MA ethics literature by assessing ethical dilemmas to provide empirical evidence about how managers would actually react to similar ethical conundrums in the workplace. Each base scenario has multiple treatments permitting detailed statistical analysis to assess influence on participant ethical judgments and planned ethical action. In short, this study will contribute to the literature because, as Brown and Treviño (2006) note, there is a substantial literature that promulgates what managers *should* do in an ethical dilemma, but relatively little evidence about what managers *would* do when faced with MA ethical quandaries. This study attempts to fill this void by examining MA professionals' perceptions of ethical dilemmas and ethical intentions in the face of such dilemmas, among other variables of interest.

## Theory Development and Key Variables

### Rest Model

Jones et al. (2003) effectively recap the Rest (1979; 1986; 1994 – hereafter Rest Model) ethical reasoning process as a four component framework where one must 1. Identify an ethical dilemma (ethical recognition); 2. Make an ethical judgment about the ethical dilemma (ethical judgment); 3. Create an intention to act ethically (ethical intentions); and 4. Act ethically (ethical behavior). Empirical research suggests the four components are generally positively associated with each other, where ethical recognition  $\Rightarrow$  ethical judgement  $\Rightarrow$  ethical intentions  $\Rightarrow$  ethical behavior (Jones et al. 2003; Johnson et al. 2012). Nevertheless, Jones (1991) clarifies

that “each component in the process is conceptually distinct and that success in one stage does not imply success in any other stage” (p. 368). The majority of ethical reasoning studies that employ the Rest Model directly test stage two and stage three, which is the design strategy that we follow because these two stages focus on participants’ assessment and reaction to the ethical dilemma posed. Furthermore, assessing Rest stage three permits one to generalize what participants’ actual behavior would be based on their ethical intentions to act, given the strong correlation between intentions to act and actual behavior (Ajzen and Fishbien 1980).

### Dependent Variables

#### *Ethical Recognition*

To measure ethical recognition we used a single item adapted from Barnett and Valentine (2004).

#### *Ethical Judgment*

To measure ethical judgment we used the first four items from the eight-item short form of the Multidimensional Ethics Scale (MES) derived from Reidenbach and Robin (1990). Reidenbach and Robin (1990) used standard scale development techniques to develop a scale that more parsimoniously measures three ethical dimensions. Flory et al. (1992) used this scale in a paper to ensure its validity. Loo (2004) also used the MES and concluded that it is psychometrically valid. McMahon and Harvey (2007) compared the eight item short form and the 30-item pool of the MES and also looked at the three factor and five factor forms of the instrument.

#### *Ethical Intention*

To measure ethical intention we used the scale from Barnett et al. 1996 that asks the participant to rate the probability that they would engage in the action themselves.

### Independent Variables

#### *Big Five*

The Big Five Personality were developed by W.T. Norman in 1963. These traits have been used across disciplines to predict human behavior. Smith et al. (2004) state that “This model is important for a few

reasons, such as: 1) it permits the sorting of personality characteristics into meaningful categories, 2) it provides a common framework and vernacular for doing research, and 3) it is supposed to cover virtually all of the personality 'space.'"

John and Srivastava (2001) concisely describe the five traits as follows:

"Briefly, **Extraversion** implies an energetic approach toward the social and material world and includes traits such as sociability, activity, assertiveness, and positive emotionality. **Agreeableness** contrasts a prosocial and communal orientation towards others with antagonism and includes traits such as altruism, tender-mindedness, trust, and modesty. **Conscientiousness** describes socially prescribed impulse control that facilitates task- and goal-directed behavior, such as thinking before acting, delaying gratification, following norms and rules, and planning, organizing, and prioritizing tasks. **Neuroticism** contrasts emotional stability and even-temperedness with negative emotionality, such as feeling anxious, nervous, sad, and tense. Finally, **Openness to Experience** (vs. closed-mindedness) describes the breadth, depth, originality, and complexity of an individual's mental and experiential life."

Extraversion has shown to be a valid predictor of training proficiency (Barrick 1991), agreeableness has been positively related to the task-oriented dimensions of leader emergence (Cogliser 2012).

Conscientiousness has consistently related to job proficiency, training proficiency, and personnel data (Barrick 1991). Openness to experience has been a valid predictor of training efficiency (Barrick 1991) as well as being positively related to the social-oriented dimensions of leader emergence (Cogliser 2012).

Openness is also correlated with being politically liberal (Carney et al 2008).

(Note: Barrick 1991 offers a good lit review with definitions, history and interpretation of each of the Big Five. Also, Stacy has a more extensive lit review on file in DropBox.)

### Care v Justice

Reiter (1996) compared the Kohlberg and the Gilligan philosophies of ethical development. Her general conclusion was that in teaching accounting ethics both theories should be used.. Because accounting

tends to be rules-based education with very limited time for personal experiential learning or for personal, ethics training, she is advocating using both care based and justice based ethical training in an ethics class in the accounting curriculum. Bay and Greenberg (2001) find that women have a monotonically increasing level of ethical behavior as the p-score on the DIT increases. They suggested that the difference between women and men in the study may be in tune with Gilligan's (1982) ethics of care, as opposed to ethics of justice.

#### *Ethics Education*

Loeb (1988) commented on teaching students accounting ethics shortly after the Treadway Commission report that encouraged ethics education in the accounting curriculum. He advocated that "classroom teaching accounting ethics may provide an accountant with confidence when approaching an ethical conflict situation." Ponemon and Glazer (1990) compared freshman, seniors and alumni from two schools: a large state university and a private liberal arts college. They found that the freshman ethical reasoning was much the same between the schools, but that the seniors and alumni from the liberal arts college had statistically significant higher ethical development than their counterparts from the large state university. They also compared their findings to findings in prior research and found that only the seniors and alumni from the liberal arts college achieved ethical development scores equal to the adult population and college graduates in general. Abdolmohammadi and Ariail (2009) found that CPAs with a graduate degree have higher ethical awareness than those with only an undergraduate degree. These studies indicate that ethics education has an effect on the ethical development and awareness of the individual. Thus, we examine if an ethics capstone class and/or if ethics discussions in accounting classes leads to more effective ethical judgement and intentions to act.

Shawver and Miller (2017) ran an experiment and determined that ethics education improve perceptions of moral intensity which in turn had an impact on moral intent. That is students reported less likelihood to complete unethical actions because they were able to recognize morally intense situations after receiving ethics training. The implications of this study are that ethics education actually have a positive effect on ethical intentions and perceptions.

### *Idealism v Relativism*

This is based on Forsyth 1980. Greenfield, Norman, and Wier (2008) and used a sample of 375 undergraduate business majors and discovered a significant relationship between an individual's ethical orientation and decision-making. They also found that participants with higher levels of professional commitment seemed less likely to engage in earnings management behavior. They used an ethics position questionnaire developed by Forsyth (1980). This questionnaire divides people into relativistic oriented versus idealistic oriented. Those that attended to be relativistic were more inclined to have their judgment modified by outcome; those that were idealistic tended to have absolute standards. (Note: these seem to me to be very similar to deontological/teleological – see if there is a literature that ties the two.)

### *Machiavellianism*

Beu and Buckley (2001) hypothesize that individuals high on Machiavellianism will be more unethical. (Note: Ford and Richardson include this in their 1994 lit review.) Hunt and Vitell (2006) briefly review Machiavellianism and moral character as it affects deontological judgments. They referred to two papers which found that low Machiavellianism, and high internal LOC is correlated with higher deontological norms. (Note: if relativism is related to deontology – then is Mach in our study correlated strongly with Relativism?) Pan and Sparks (2012) showed in their meta-analysis that as Machiavellianism increases, ethical judgments become less strict.



### *Moral Intensity*

Jones (1991) theorized that characteristics of the actual moral issue itself can impact ethical judgments as well as ethical intentions. Specifically, some ethical dilemmas are more highly ethically charged than other dilemmas, so Jones created a moral intensity construct that accounts for ethical differences in business ethics situations while also capturing the issue contingent moral imperative nature of the dilemma. The six component moral intensity construct does not attempt to measure the moral development of the ethical decision maker and also does not attempt to capture the ethical culture of the organization. Salience and vividness will both increase moral intensity. Moral intensity has six facets<sup>1</sup>:

1. Magnitude of consequences, defined as the sum of the harm. An action that causes the greatest harm to the most people has the greatest magnitude and thus will elicit greater effort during decision making. If the harm doesn't meet some threshold, the agent may fail to recognize the moral issue at all.
2. Social consensus refers to the amount of good or evil the relevant society places upon the act, it also refers to the legality of the act.
3. Probability of effect refers to whether the act will happen or not and if it does whether the harm will actually occur. This is balanced against the magnitude of the gain. This tends to be an expected value calculation.
4. Temporal immediacy indicates that the consequences of the moral action will occur sooner rather than later, causing greater salience.
5. Proximity is the feeling of nearness either geographically, socially, culturally, or psychologically. If negative consequences will happen to those with whom we share greater proximity, we are less likely to develop unethical intent. The opposite of proximity is dispersion or distance.
6. Concentration of effect is an inverse function of the number of people affected by an act of given magnitude.

Moral intensity has been assessed in previous accounting ethics studies (Morris and McDonald 1995; Singhapakdi et al. 1996; Shaub 1997; Wright, Cullinan and Blin 1997; Jones et al. 2003;

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<sup>1</sup> These are quoted and/or paraphrased from Jones 1991 pages 374-378.

Leitsch 2004; Fleischman et al. 2010; Coram, Glavovic, Ng, and Woodliff 2008; Ng, White, Lee, and Moneta 2009).

We contend that moral intensity is a critical predictor variable for the present inquiry because morally intense situations become “the proving ground for ethical leadership” (Brown and Treviño 2006, p.602). It is important to investigate moral intensity because it permits one to specifically identify what scenario issues participants perceive to be especially salient. Brown and Treviño (2006, p. 602) describe further the following regarding moral intensity in general, and the dimension of magnitude of consequences in particular.

[These concepts are] particularly important for ethical leadership because ethical leaders consider the consequences that their potential actions will have on others. When the potential for great harm exists, observers will pay attention to the decision maker to see how he or she handles the situation. When leaders face situations that have the potential to cause great harm and handle them in an ethically appropriate manner (as judged by followers), then the leader will be seen as an ethical leader. On the other hand, when leaders make decisions that bring significant harm to others, they will be seen as poor models of ethical behavior.

The literature indicates that the moral intensity scale theoretically strengthens ethical judgments as well as ethical intentions (Jones 1991; Jones et al. 2003; Brown and Treviño 2006; Fleischman et al. 2010), meaning that moral actors who perceive morally intense situations should all else equal engage in more effective ethical reasoning. This contention is supported by previous cross-sectional empirical ethics research in accounting (e.g. Jones et al. 2003; Fleischman et al. 2010).

#### *Perceived Importance of an Ethical Issue (PIE)*

Another key ethics construct that augments moral intensity is PIE, which was developed by Robin et al. (1996). They contend that PIE enhances ethical judgment and ethical intention, the second and third steps of the ethical reasoning process, respectively. Other studies also suggest

that PIE appears to consistently impact ethical judgments and intentions (Cronan, Leonard, and Kreie 2005; Haines, Street, and Haines 2008), much in the same manner as issue recognition. Therefore, we believe it is a key variable in this MA ethical dilemma study.

#### *Religiosity*

Allport and Ross (1967) that found that intrinsic religiosity increases or is correlated with increased deontological judgment, whereas extrinsic religiosity is not. Emerson, Conroy and Stanley (2007) claim that religiosity is a key indicator of ethical attitude based on a national survey of 5,000 AICPA members with a 10.4% response rate. Pan and Sparks (2012) show that as religiosity increases, ethical judgments become stricter. Walker et. al (2012) found a general religiosity was correlated with accepting morally questionable actions where as intrinsic religious motivation was negatively correlated perceptions of loving God also negatively correlated and extreme extrinsic religious motivations were positively correlated with accepting questionable actions. This agrees with Allport and Ross (1967) but contradicts Conroy and Stanley (2007).

#### *Political Orientation*

Etherington and Hill (1998) found those classifying themselves as conservative have significantly lower moral reasoning than those classifying themselves as liberals or moderates. The authors note that finding more conservative political positions been correlated with lower ethical reasoning is disturbing since about two thirds of the CMAs were self-professed conservatives. Jones et al (2003) found evidence that political orientation affects judgment.

#### *Social Desirability Bias*

Social desirability bias is usually a concern in ethics research (Randall and Fernandes 1992; Cohen, Pant and Sharp 1996, 2001; Fleischman et al. 2007; 2010; Cohen, HolderWebb, Sharp, and Pant 2007; Johnson et al. 2012) because participants in ethically charged situations tend to present themselves in a socially desirable manner, meaning that they do not want to

admit that they would act unethically. To measure this we followed Cohen et al. (2007, p. 1126) by calculating social desirability as the difference between ethical intentions where participants were asked the probability that their peers would act the same as the vignette actor versus how the participant themselves would act using the same four-item, 7-point Likert ethical intentions scale (Barnett, Bass, and Brown 1996). Averages for each set are calculated and then the difference taken for a score consistent with Cohen et al. (2007).

#### *Societal Norms*

Based on Barnett 1999.

#### *Utilitarianism*

Treviño, Weaver and Reynolds (2006) did a literature review of behavioral ethics, including utilitarianism. Re-read this if it is a significant variable.

### **Experiment**

The study employs two base MA scenarios that are presented in the Appendix. Scenario 1 focuses on an assistant controller, Jones Williams, who initially authorized repairs deemed essential to enhancing operational efficiency in order to entice a large new client. However, because of transaction complications and delays, the firm was unable to obtain the new business as fast as it would have liked, resulting in disappointing first quarter results. Unfortunately, the poor financial performance triggered by the additional repairs would cause the company to become out of compliance with debt covenants, which will necessitate additional collateral that would be difficult to finance. Due to these pressures from the bank, and given that Jones wanted to apply for the vacant controller position, Jones decides to capitalize the expenses instead of correctly recording them as revenue expenditures. This reclassification helps the firm avoid debt covenant noncompliance. This scenario has a 2 X 2

randomized design with the manipulations ethical versus unethical and favorable versus unfavorable personal outcome. For the pilot study we only tested the version of the scenario that showed unethical actions on the part of Jones due to the small number of participants.

Scenario 2 features Smith Miller, one of three senior managers submitting internal proposals for potential capital budget funding. Only one manager is selected each year to receive funding up to one million dollars. The last three managers that won the bid and completed their projects successfully were promoted to vice president and given very handsome salary increases. At the end of the cost analysis, Smith realizes that the project's proposed Internal Rate of Return (IRR) is estimated to come in at 7.5%, but every project approved in the last few years had an 8% IRR or higher. Smith realizes that by reclassifying one project expenditure as a normal operating expense instead of a project expense, the projected IRR could be adjusted upwards to 8.15%. This higher IRR would improve the likelihood of getting the funding and the cost reclassification to operations is unlikely to be discovered. The purpose of this second base scenario is to assess participant perceptions that relate to a reclassification that does not result in a very large upward adjustment in IRR.

Scenario 3 is a slight variation on Scenario 2. It involves a cost reclassification that results in a much larger upward adjustment in IRR. In Scenario 3, River Wilson is substituted for Smith Miller above, but plays an indistinguishable role. The scenario is virtually identical to Scenario 2 above except that every project approved in the past had an IRR of 10% or above, rather than 8% in Scenario 2. River's Scenario 3 cost reclassification results in an upwards

adjustment in IRR from 7.5% to 10.15%, rather than only to 8.15% in Scenario 2. The difference between these two magnitudes offers a different level of moral intensity.

Both Scenario 2 and Scenario 3 involve a randomized 2 X 3 design. The first manipulation is ethical versus unethical behavior. The second is outcome as follows:

- a. favorable consequences where the reclassification produces a much larger return than projected, allowing the moral agent to reverse the initial reclassification,
- b. favorable consequences where the reclassification produces the expected return when no reversal is recorded, and
- c. unfavorable consequences.

In the pilot study we only looked at unethical behavior by the actor due to a small number of participants.

### Analysis

The study employs General Linear Modeling (GLM) MANCOVA regression because this multivariate statistical method efficiently assesses correlated dependent variables, consistent with previous research in accounting (Fleischman and Stephenson 2012; Johnson et al. 2012). MANCOVA permits us to statistically assess the impact of our predictor variables on our two correlated dependent variables simultaneously. Furthermore, MANCOVA is appropriate when there is a mix of nonmetric categorical predictor variables (coded as fixed factors), combined with metric ordinal or continuous variables (coded as covariates). Fleischman and Stephenson (2012, p. 426, footnote 7) highlight that MANCOVA is especially efficient in minimizing type 1 errors while also increasing the likelihood of finding significant predictor variable associations

as compared with univariate assessment. MANCOVA regression will address how moral intensity influences ethical judgements as well as ethical intentions.

We will also use independent samples *t* tests with correction for unequal variances to investigate the interplay between ethical (unethical) behavioral treatments with favorable (unfavorable) consequence treatments on moral intensity. Independent sample *t* tests also assess treatment interplay to identify the moderating influence on ethical judgments and ethical intentions.

### Preliminary (2<sup>nd</sup> Pilot) Results

We ran a pilot study of Scenario 2 and 3 vignettes at a large southeastern university with graduate students, many of whom work or have worked in management. The purpose of this pilot was to determine if there are statistical differences between the vignettes and if the variables of interest are significantly correlated with our dependent variables (ethical judgment and ethical intention).

Running two-sample *t*-tests between each version of the two vignettes and between the related treatments showed few statistically significant results. This indicates that we need to carefully review the manipulations and adjust the instrument.

We employed GLM MANCOVA regression to determine the significance of predictor variables. Because all predictor variables must be significant in the multivariate model, any that were not significant were dropped. The results of the analysis reduced model are shown in Table 1. Our preliminary results show that having teleological leanings greater PIE are strongly associated with ethical judgment. Additionally, greater moral intensity is weakly associated with ethical judgment. Our participants show nominal social desirability bias when exercising ethical

judgment, but a great deal when indicating an ethical intention. Moral intensity also is moderately associated with ethical intention. Discussing ethics in a greater percentage of accounting classes did not significantly affect ethical judgement, but it did moderately affect ethical intention. Finally, both teleological leanings and greater PIE were weakly associated with ethical intention.

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Table 1

## Univariate Analysis of Covariance (ANCOVA)

Panel A: Dependent Measure = Ethical Judgment (adjusted  $R^2 = .465$ )

Source	MS	F		Partial $\eta^2$	Power
Corrected Model	24.917	20.411	***	.489	1.000
Intercept	13.870	11.362	***	.082	.917
Moral Intensity	4.033	3.304	^	.025	.438
Social Desirability	1.012	.829		.829	.148
Teleological	14.330	11.739	***	.084	.925
PIE	48.165	39.455	***	.236	1.000
Ethics Classes	1.640	1.344		.010	.210
Treatment	4.132	3.385	^	.026	.447

Panel B: Dependent Measure = Ethical Intention (adjusted  $R^2 = .322$ )

Source	MS	F		Partial $\eta^2$	Power
Corrected Model	12.822	11.623	***	.353	1.000
Intercept	13.736	12.450	***	.089	.938
Moral Intensity	9.022	8.178	**	.060	.810
Social Desirability	13.274	12.032	***	.086	.931
Teleological	3.529	3.199	^	.024	.427
PIE	3.233	2.930	^	.022	.397
Ethics Classes	4.475	4.057	*	.031	.516
Treatment	.927	.840		.007	.149

Note: ^, \*, \*\*, and \*\*\* represent significance levels of 0.10, 0.05, 0.01, and 0.001, respectively.

## Appendix A

### Survey Materials

#### SCENARIO 1: (Manager-improper journal entries)

FSW's assistant controller, Jeff/Julie Jones, authorized repairs necessary to enhance the efficiency of operations to entice a large new client to move its business to FSW. Jones knew that the new business resulting from the client would offset the cost of repairs. Unfortunately, complications delayed the transition, and disappointing first quarter results were in. The shareholders and managers would be upset, of course, but the real problem was National Bank. The loan covenants were out of compliance due to the increased expenses; thus, additional collateral would be required and a large payment would have to be paid. Jones wasn't sure what assets were available for collateral, but was sure that free cash flow wasn't sufficient for the payment. Jones, up for promotion to the vacant controller position, knew the repairs started a chain of events that might seriously jeopardize the promotion. Jones scanned the records again and realized that a simple journal entry reclassifying one of the repairs as an asset would put the quarterly results on target and prevent issues with the loan covenants. Next quarter, when the new business comes in, that entry can be reversed and the overall results for the first half of the year will be accurate.

##### **Ethical-Favorable (Treatment 1A)**

**Behavioral Action:** After thinking the situation through, Jones decided to not make the journal entry. Instead Jones chose to write an explanation for the bank in an effort to secure an extension on the loan covenants.

**Consequences of Behavioral Action:** The bank agreed that it was a temporary situation and gave a 90-day extension to the covenants. FSW's CEO, impressed with how Jones handled the situation, approved the promotion to controller and a pay raise.

##### **Unethical-Favorable (Treatment 1B)**

**Behavioral Action:** After thinking the situation through, Jones decided to make the journal entry. The next quarter the client was brought onboard, the journal entry reversed and the quarterly results were as anticipated.

**Consequences of Behavioral Action:** FSW's CEO, impressed with how Jones handled the situation, approved the promotion to controller and a pay raise.

##### **Ethical-Unfavorable (Treatment 1C)**

**Behavioral Action:** After thinking the situation through, Jones decided to not make the journal entry. Instead Jones chose to write an explanation for the bank in an effort to secure an extension on the loan covenants.

**Consequences of Behavioral Action:** The bank did not care that it was a temporary situation and gave FSW 10 days to provide additional collateral and make a large payment. FSW's CEO, distressed with how Jones handled the situation, issued a reprimand and removed Jones' name from the pool of candidates for controller.

##### **Unethical-Unfavorable (Treatment 1D)**

**Behavioral Action:** After thinking the situation through, Jones decided to make the journal entry. The next quarter the client was brought onboard, the journal entry reversed and the quarterly results were as anticipated.

**Consequences of Behavioral Action:** However, Jones' colleague informed the CEO of Jones' actions. FSW's CEO, distressed with how Jones handled the situation, issued a reprimand and removed Jones' name from the pool of candidates for controller.

## **SCENARIO 2: (Manager-improper estimates/capital budgeting/small variance)**

Paul/Paula Smith is one of three senior managers submitting internal proposals for a capital budgeting project. Only one manager is selected each year to receive funding that can reach up to one million dollars. The last three managers that won the bid were promoted to vice president and given very handsome salary increases. Smith asked each member of the department to gather information on projected costs and revenue, and was assembling the pieces into a final project budget. At the end of the analysis, Smith stared at the computer in disbelief. The Internal Rate of Return (IRR) was estimated to come in at 7.5%, but every project approved in the last few years had an 8% IRR or higher. Smith examined the numbers for a long time and realized that by reclassifying one project expenditure as a normal operating expense instead of a project expense, the projected IRR could be adjusted upwards to 8.15%. Smith knew the higher IRR would improve the likelihood of getting the funding and the cost reclassification to operations was unlikely to be discovered.

### **Unethical-Favorable-Lower Operating Income (Treatment 2A)**

**Behavioral Action:** Smith decided to turn in the proposal based on the higher projected IRR due to the cost reclassification. **Consequences of Behavioral Action:** The project was funded and, when completed, the IRR came in at 8%. No one noticed the added expenditure that had been reclassified to normal operations, thus understating operating income. One year later Smith was promoted to vice president.

### **Unethical-Unfavorable (Treatment 2B)**

**Behavioral Action:** Smith decided to turn in the proposal based on the higher projected IRR due to the cost reclassification. **Consequences of Behavioral Action:** The project was funded and, when completed, the IRR came in at 8%. During the annual audit a few months later, the project expenditure that had been reclassified to normal operations was discovered and reassigned to the project. The IRR for the project was recalculated to be 7.4%. Smith was not promoted.

### **Unethical-Favorable – Higher Operating Inc. (Treatment 2C)**

**Behavioral Action:** Smith decided to turn in the proposal based on the higher projected IRR due to the cost reclassification. **Consequences of Behavioral Action:** The project was funded and, when completed, the IRR came in much higher than expected. Smith was able to reverse the reclassification by reinstating the omitted expenditure back to the project rather than normal operations and still achieve an IRR of 8% on the project. One year later Smith was promoted to vice president.

**Next is a set of adjectives that allow you to share your overall general beliefs about the situation/ issue above regarding [Name of Actor]'s behavioral action.**

1. FAIR -- UNFAIR
2. JUST -- UNJUST
3. MORALLY RIGHT -- NOT MORALLY RIGHT
4. ACCEPTABLE TO MY FAMILY --UNACCEPTABLE TO MY FAMILY
5. UNIMPORTANT ISSUE --IMPORTANT ISSUE
6. INSIGNIFICANT ISSUE --SIGNIFICANT ISSUE
7. ISSUE IS OF NO CONCERN -- ISSUE IS OF CONSIDERABLE CONCERN
8. TRIVIAL ISSUE--FUNDAMENTAL ISSUE
  
9. I believe this scenario overall involves an ethical dilemma: DISAGREE -- AGREE
  
10. I believe [Name of Actor]'s behavioral actions overall are: VERY UNETHICAL -- VERY ETHICAL

The probability I would behave the same way as [Actor]:

11. LIKELY -- UNLIKELY
12. IMPROBABLE -- PROBABLE
13. POSSIBLE -- IMPOSSIBLE
14. DEFINITELY WOULD NOT -- DEFINITELY WOULD

The probability my peers would behave the same way as [Actor] is:

15. LIKELY -- UNLIKELY
16. IMPROBABLE -- PROBABLE
17. POSSIBLE -- IMPOSSIBLE
18. DEFINITELY WOULD NOT -- DEFINITELY WOULD

19. If I were [Actor]'s spouse, I would offer the following advice:

20. The scenario above involves an assistant controller who is trying to decide whether or not to reclassify repairs expense as an asset.

**Yes\_\_\_ No \_\_\_ (please check one)**

21. The scenario above involves an assistant controller who is trying to decide whether or not to reclassify repairs expense as an asset.

**Yes\_\_\_ No \_\_\_ (please check one)**

**Below is a set of questions about your attitudes and opinions regarding the scenario above. Use the following response scale and write the number that indicates your level of agreement with each statement in the space provided. Strongly Disagree=1 to Strongly Agree=7**

22. The overall harm (if any) from [Actor]'s behavioral action would be very small.
23. Most people would agree that [Actor]'s behavioral action is wrong.
24. There is a very small likelihood that [Actor]'s behavioral action will actually cause any harm.
25. [Actor]'s behavioral action will not cause any harm in the immediate future.
26. If [Actor] is a personal friend with people at National Bank, the behavioral action is wrong.
27. [Actor]'s actions will harm very few people (if any).
28. It is important to do the right thing, even if one's self and/or family suffer greatly as a result.
29. Before knowing the consequences of an action, it can be said to be either right or wrong.



30. It is wrong to decide whether or not to perform an act by balancing the act's positive consequences against its negative consequences.
31. Some actions are simply wrong, even though they may result in positive consequences for many people.
32. There are important rules determining whether an action is right or wrong that do not depend on the consequences of the action.
33. It is not possible to determine the rightness or wrongness of an action without considering the consequences.
34. A right action is one that provides the greatest good for the greatest number of people.
35. A right action is one that provides the greatest good for me, my family, and those for whom I care greatly.
36. As the probability of positive consequences resulting from an action increases, the action increasingly becomes the right thing.
37. People should make sure that their actions never intentionally harm another even to a small degree.
38. Risks to another should never be tolerated, irrespective of how small the risks might be.
39. The existence of potential harm to others is always wrong, irrespective of the benefits to be gained.
40. One should never psychologically or physically harm another person.
41. One should not perform an action which might in any way threaten the dignity or welfare of another individual.
42. If an action could harm an innocent other, then it should not be done.
43. Deciding whether or not to perform an act by balancing consequences of the act against the negative consequences of the act is immoral.
44. The dignity and welfare of the people should be the most important concern in any society.
45. It is never necessary to sacrifice the welfare of others.
46. Moral behaviors are actions that closely match ideals of the most "perfect" action.
47. There are no ethical principles that are so important that they should be a part of any code of ethics.
48. What is ethical varies from one situation and society to another.
49. Moral standards should be seen as being individualistic; what one person considers to be moral may be judged to be immoral by another person.
50. Different types of morality cannot be compared as to "rightness".
51. Questions of what is ethical for everyone can never be resolved since what is moral or immoral is up to the individual.
52. Moral standards are simply personal rules that indicate how a person should behave, and are not to be applied in making judgments of others.
53. Ethical considerations in interpersonal relations are so complex that individuals should be allowed to formulate their own individual codes.
54. Rigidly codifying an ethical position that prevents certain types of actions could stand in the way of better human relations and adjustment.
55. No rule concerning lying can be formulated; whether a lie is permissible or not permissible totally depends on the situation.
56. Whether a lie is judged to be moral or immoral depends upon the circumstances surrounding the action.
57. Never tell anyone the real reason you did something unless it is useful to do so.
58. It is wise to flatter important people.
59. It is hard to get ahead without cutting corners here and there.
60. The best way to handle people is to tell them what they want to hear.
61. Anyone who completely trusts anyone else is asking for trouble.
62. I pray at least once weekly.
63. I attend a religious service (church, temple, mass, mosque) at least once every three months.
64. I consider myself to be politically liberal.

**Listed below are a series of statements about your actions. True/False.**

65. I like to gossip at times.
66. There have been occasions when I took advantage of someone.
67. I'm always willing to admit it when I make a mistake.
68. I always try to practice what I preach.

69. I sometimes try to get even, rather than forgive and forget.  
70. At times I have really insisted on having things my own way.  
71. There have been occasions when I felt like smashing things.  
72. I never resent being asked to return a favor.  
73. I have never been irked when people expressed ideas very different from my own.  
74. I have never deliberately said something that hurt someone's feelings.
- 

**The following information will be used for classification purposes only and will remain confidential and anonymous.**

Your age? \_\_\_\_\_ years old Your sex? (please circle) Male Female

Year in school (freshman, sophomore, etc.)? \_\_\_\_\_

Have you taken a course that was specifically designed to fill an ethics requirement? Yes No

Major (accounting, marketing, etc.)? \_\_\_\_\_ Minor? \_\_\_\_\_

Are you a transfer student? \_\_\_\_\_ If yes, did you transfer from a community college within Kentucky?

In what percent of your business classes did your instructors explicitly talk about ethics?

\_\_\_\_\_ 0 – 10% \_\_\_\_\_ 11 – 25% \_\_\_\_\_ 26 – 50% \_\_\_\_\_ 56 – 75% \_\_\_\_\_ 76 – 100%

Total years of experience working in your current field(s) of study? \_\_\_\_\_

Total years of experience working in any job? \_\_\_\_\_

What is your marital status? (please check) \_\_Single \_\_Widowed \_\_Married \_\_Separated, Divorced

What is your race? (please check)

\_\_\_\_\_ Black/African American \_\_\_\_\_ White/Caucasian

\_\_\_\_\_ Asian \_\_\_\_\_ American Indian

\_\_\_\_\_ Other (please specify) \_\_\_\_\_ Prefer not to answer

\_\_\_\_\_

What geographic region do you consider home? (please check)

\_\_\_\_\_ West \_\_\_\_\_ Northeast \_\_\_\_\_ Southwest

\_\_\_\_\_ Midwest \_\_\_\_\_ South \_\_\_\_\_ Other (please specify) \_\_\_\_\_