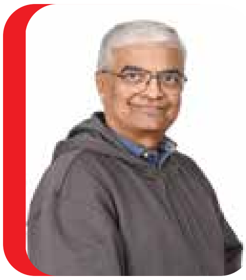
AUDITORS & ACCOUNTANTS AND BUSINESS ETHICS

Abstract

Ensuring the legality and accuracy of the business transactions is a primary responsibility of the auditors and accountants. This responsibility becomes difficult when the business owners and their senior executives indulge in 'ethical flexibility' i.e. a manipulative transactional behaviour. This article assesses this complexity and presents a pragmatic solution.



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Businesses cannot be separated from the society. Therefore, it is very natural that the ethical standards of a society also influence the ethical parameters of conducting business. Largely the ‘ethos of a business enterprise’ is made of the ethics practiced by its various stakeholders, mainly the owners. Business ethics are a combined result of the quality of corporate governance, enterprise governance and family governance. In India, eighty five percent of business enterprises are closely owned by business families and hence the family’s ethical norms substantially define the ethos of a business organisation. Auditors and accountants basically perform within the boundaries defined by this ethos. Higher the ethical quality of this ethos, better the performance of the accountants and auditors. Yet defining business ethics could become difficult because separating the manipulations from the frauds could be difficult. Also the intensity of the role of the regulatory bodies may differ in different countries. For example, in one country a business offence may be viewed as ‘lesser unethical’ and hence the punishment may not be very harsh. The same offence in another country may attract imprisonment. There is another complexity the auditors and accountants face - differentiating between legality and morality. We do not have well defined standards which separate ‘legal accounting’ from ‘ethical accounting’. We take legality as ethical, although it may not be so. Hence different business enterprises practice different combinations of being ethical and also being legal.

The weekly issue of a very reputed international magazine, published a news about an international audit firm. Employees of this audit firm cheated in their examination on ethics. The firm was fined by the Securities and Exchange Commission, to the tune of hundred million dollars. Basically, the very role of an auditor is to vouch business irregularities & frauds and report them to the regulatory bodies, shareholders and other concerned institutions & stakeholders. But unfortunately, in many companies, if the owners themselves (directly & indirectly) appoint these auditors every year, then how would it be possible for them to disclose the frauds of their bosses? Of course, a lot has been spoken and written about this fact. This article attempts to discuss the limitations of the auditors and accountants in the context of ‘Ethics in Business’. Many business frauds, sins and irregularities do not come into the purview or investigative inquiry to be conducted by the auditors & accountants. In other words, auditors too cannot do much about certain serious matters in and outside the boundaries of corporate governance. The 'whistle blowers' who expose the frauds committed by the powerful people, are the real warriors. But these are a very small number. Many of us prefer to remain silent than speak out, for either we are coward or insensitive or our monetary interest is involved. (Ironically today such a behaviour is defined as pragmatic and practical!)

If the ethical performance of the auditors and accountants is to be completely assured, then we need to use "Versatile Accounting" i.e. "Integrated Accounting". This integration should offer multiple types and levels of benchmarks. The business performance should be monitored through four types of benchmarks viz. strategic, managerial, operational and financial. These four control systems should be intelligently connected with each other, so that the scope for any manipulation is minimised. This combination should offer multiple cross-checks so that vouching of governance - related lapses should be easily possible. Strategic accounting should facilitate 'Policy Audit' and Management Accounting should support 'Management Audit'. If the equilibrium of all the three types of governance is well maintained, the auditors' job would become easy. Ultimately the ethical conduct of accounting and auditing would depend on the quality of family governance.

Those industrialists who grow exponentially in a very small period of time, mostly could do so either with government's patronage or unethical shortcuts. Business - related corruption has been there all the time worldwide. Earlier the politicians and bureaucrats were bribed to take undue advantage of the loopholes in the law. Now the law itself is changed in many countries by these cronies. What can the auditors and accountants do about this systematically legitimised corruption? Those mighty corrupt industrialists who destroy competition & create their unchecked monopoly, compel government to discard the subsidies offered to the poor and increase budgetary provision for their concessions, create unproductive assets for the banks by not paying their loans, destroy the primary rights of the tribals, exploit the natural resources and get all these sins legalised to establish their industrial empires, do not simply bother about audits and public scrutiny. Unless a fair and transparent "Policy Audit" is conducted and the complete truth is presented before the public, such mammoth sins cannot be punished appropriately. If the 'policy auditors' too are vulnerable to corruption, then there is something seriously wrong with the character of the nation. Such characterless nations march rapidly towards doom and the 'poor common people' pay a hefty price for it.

Business organizations do conduct 'Strategy Audit'. It is supplemented by 'Management Audit'. These audits verify the validity of each strategy and vouch the management of its execution respectively. These internal audits are to be primarily supervised by the 'independent directors' of a company. Here again we need to raise the same earlier point - "If these independent directors are appointed by the powerful owners, how are they going to use their independence?" Most of these so-called audit reports cover up the sins and blunders of the owners and top executives. A lot of vagueness is deliberately orchestrated in these reports when they are being prepared. The owners and independent directors often shamelessly & cunningly accept that they are incompetent but definitely not fraudsters. Penalty for an incompetency is far lesser than the punishment for a fraud. The line of demarcation between an error and a sin is very often not so clear. Fraudsters always take an undue advantage of this ambiguity. In a few crony capitalist countries, a serious offence can be pardoned if the offender pays a hefty financial penalty. So, if you are very wealthy and can afford to pay such a hefty penalty, then you are eligible to indulge in a serious crime! What should an auditor do about this, who investigates and exposes such serious crime?

Many business owners compel their accountants to manipulate the accounts, in order to evade taxes, hide true profit from the partner, pay lesser salary to the employees and load their personal expenses to the business. The poor, helpless accountants obey their master to save their job. Manipulation is an unethical act conducted within a legal frame. Not everything is black and white in accounting & finance. Here a lot of subjectivity is cleverly used for doing manipulations. If at all these manipulators are caught, they escape through the routes of penalties and bribes. Of course, a good amount of innocence is played here too, to escape. The owners put the blame on the accountants. Many industrialists (and even the small businessmen) get manipulations done through their accountants because they are not afraid of the 'system' or they are confident enough to buy the 'system'. By evading a tax of hundred rupees, they feel that they can comfortably spend twenty rupees on penalties & bribes. This proves to be a very convenient 'cost - benefit analysis' for them! The sad irony here is, these same tax - evaders make big claims of patriotism in the social media and lecture the students of accounting & auditing on 'business ethics'.

Auditors are mainly expected to verify and ascertain a neat execution of the accounting & budgetary processes. This verification includes the compliance of accounting law, the spending authority of the directors & executives, budgetary provisions, tax laws and other relevant details. While doing so the main focus is on a comparison between the budgeted expenditure and the actual expenditure. The statutory or external auditors are not generally responsible to assess the validity of a budgetary provision by using the market benchmarks. They mostly use the data that is provided to them. Therefore, the nature of their work is that of a 'defined & limited scrutiny'. This scrutiny is not expected to be very versatile, complete on all the maximum possible strategic & operational parameters and subject to different definitions of morality. Quite a few auditors are not supposed to be educated about or aware of a complex correlation between a technical or strategic parameter and a corresponding financial parameter. A company's directors and top executives often take undue advantage of this limitation of an auditor's knowledge and role. For example, financial auditors are not expected to know thoroughly the process of deep-sea crude oil exploration, its risks & uncertainties, technological complexity etc. This is actually a domain area of very special technical and strategic audit. There is no exact and formal definition of the social accountability of these specialist auditors, so that they can be held answerable to the common people.

Our overall collective morality of public life has terribly deteriorated. Our parameters of morality are a matter of subjective convenience and connivance. Everyone as per his convenience, is painting these parameters with different philosophical colours. There is a big chaos around us. The mighty corrupt industrialists are exploiting this chaos to their advantage. Different power groups are shielding the corruption of these crony capitalists because all of them are the beneficiaries. Who will audit this horrible chaotic situation? If the public is sovereign, what type of audit would safeguard this sovereignty? Can the corrupt industrialists be held accountable to public? Are they truly auditable? Today governments of many countries are influenced by the business empires. Government budgets and public policies are under the terrible clout of these empires. Because this crony influence could not be timely and fully audited, economies of some of the powerful nations are in serious trouble today. Of course, the beneficiary groups from these nations won't accept this sad reality. Basically, people do not have appropriate parameters to audit the relationship between the industrialists, government and other elements. Today world over the people's sovereignty is in a serious danger. Those mighty cronies who should be held accountable, answerable and auditable to the general public are mostly free from every check and control. Therefore, we should basically audit the present system and the situation around us and not merely blame the helpless auditors who enjoy very limited power and possess an inefficient mechanism to check the business ethics.