

## Hypothetical: Auditing Financial Statements

### Situation One

- **Year 1:** Auditor reviews and approves accurate, ethical statement.
- **Year 2:** Same as previous year.
- **Year 3:** Same as previous year.
- **Year 4:** Company stretched legal limits, possibly breaking some.

Expected auditor response?

### Situation Two

- **Year 1:** Auditor reviews and approves accurate, ethical statement.
- **Year 2:** Company position aggressive but doesn't violate law. Auditor approves.
- **Year 3:** Company position even more aggressive but still not illegal. Auditor approves.
- **Year 4:** Company stretched legal limits, possibly breaking some.

Same response?

*This slide and the next two are a module designed for insertion into a government ethics presentation. They are intended to sensitize audiences to the very real danger that exposure to a gradual erosion of ethical standards is contagious.*

*Show this slide, providing enough information so that everyone understands the hypothetical, and then ask:*

OK, what do you think?

Does anybody think that the auditors in this hypothetical confronted with a gradual deterioration of ethical standards are less likely to maintain their own standards, right? Is that a justified belief?

Well, guess what? We are not the only ones who recognize the danger. Two Harvard Business School professors published an article about this very issue in the *Journal of Experimental Social Psychology*. [Show next slide].

**Admin Notes:** *Comments in a regular font are intended as an optional script for presenters. Comments in regular type are background information for the presenter. The slide uses no graphics, since it will be normally adopt the template of the slide show that contains it.*

# Gradual Ethical Standard Erosion

## Source of Hypothetical

Gino and Bazerman, "When Misconduct Goes Unnoticed: The Acceptability of Gradual Erosion in Others' Unethical Behavior."

[45 Journal of Experimental Social Psychology 708](#) (2009).

## Authors (Both Harvard Business School)



Prof. Francesca Gino



Prof. Max Bazerman

*Quote from Gino/Bazerman article or paraphrase as desired:*

For an illustration of this argument, imagine that an accountant employed by a well-known accounting firm is in charge of the audit of a large corporation with a strong reputation. The accounting firm and the client have an excellent relationship, and the accounting firm receives tens of millions of dollars in fees from the client each year. For 3 years, the accountant in charge of the audit viewed and approved the client's high-quality, ethical financial statements. Suddenly, in the fourth year, the corporation stretches the limits of the law, and even breaks it in certain areas. Would the accountant sign a statement certifying that the financial statements were acceptable according to government regulations? Now suppose that the accountant saw and approved of the company's high-quality, highly ethical financial statements for 1 year. The following year, the corporation begins stretching the law in a few areas, without appearing to break the law. In the third year, the firm stretches the ethicality of its returns a bit more. Some of the company's accounting decisions now possibly violate federal accounting standards. By the fourth year, the corporation stretches the limits of the law in more areas and occasionally breaks the law.

We believe that the accountant is much less likely to refuse to sign the

The screenshot shows the top portion of a Washington Post article. The masthead includes 'The Washington Post' and navigation links for PostTV, Politics, Opinions, Local, Sports, National, World, and Business. The main headline reads: 'Report: DHS employees abusing overtime allowances, being paid for time not necessary for jobs'. Below the headline is a sub-headline: 'WASHINGTON — Employees from six Homeland Security Department offices have abused an overtime program and cost the government about \$8.7 million a year, according an Office of Special Counsel letter and report sent Thursday to the president and Congress.' The article text continues: 'Special Counsel Carolyn Lerner told President Barack Obama and lawmakers that whistle-blowers alerted her office to the abuses. Lerner's letter and an accompanying report detailed allegations of overtime abuses in Washington. She said her office is investigating five other overtime abuse cases and expects the allegations to be substantiated.' A small image of a person is visible on the left side of the article.

## DHS Overtime Scandal

DHS employees receive \$8.7 million a year in overtime pay for:

- Watching television
- Surfing the Internet
- Relaxing at their desks

This was a front page story in the November 2, 2013 Washington Post. Yeah, that's \$8.7 million a year. For watching television, surfing the Internet or just hanging out.

One question for you: How many people here think that situation like this developed overnight?

Maybe those professors really are onto something? When the ethics standards of those around us degrade slowly, there is a real risk that we will become less likely to object, or even lower our own standards. It's like the proverbial frog boiling to death in a saucepan. He's dead before he realizes he's in danger.

[http://www.washingtonpost.com/national/report-dhs-employees-abusing-overtime-allowances-being-paid-for-time-not-necessary-for-jobs/2013/10/31/7aa421ba-428d-11e3-b028-de922d7a3f47\\_story.html?tid=auto\\_complete](http://www.washingtonpost.com/national/report-dhs-employees-abusing-overtime-allowances-being-paid-for-time-not-necessary-for-jobs/2013/10/31/7aa421ba-428d-11e3-b028-de922d7a3f47_story.html?tid=auto_complete)

*Employees from six Homeland Security Department offices have abused an overtime program and cost the government about \$8.7 million a year, according an Office of Special Counsel letter and report sent Thursday to the president and Congress. Special Counsel Carolyn Lerner told President Barack Obama and lawmakers that whistle-blowers alerted her office to the abuses.*