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Unethical issues in accounting: A case study of India

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Abstract: Accounting being the backbone of any firm must go hand in hand with ethics, but unfortunately it has not. In current scenario, when the world is witnessing numerous accounting scams, following ethics in accounting has become a prerequisite. This research paper mainly focuses on the role, the ethics play in the accounting profession. To address this issue, the inferences were taken from Satyam scam and the failures of the corporate ethics and lessons learnt are analysed. Finally few suggestions and measures to contain such scams in future are also provided in the interest of stakeholders by considering the importance of good Corporate Governance.

Methodology: The study here is primarily based on secondary data collected from relevant literature published in the journal, newspapers, websites, books, reports etc.

Conclusion: Few suggestions and measures are discussed so that the accounting regulating bodies and government in India can keep an eye on unethical behaviour of management & auditors to minimise such type of accounting scams in future.

Keywords: Accounting, Ethics, Satyam Scam, Corporate Governance

Abbreviations: AICPA (American Institute of Certified Public Accountant), IIA (institute of internal auditors), IMA (institute of management accounts)

I. Introduction

A. Accounting

Accounting simply refers to the process of recording, presenting, analysing and communicating the financial information regarding financial position and operation profitability of the business firm to its users. This information is vital as it helps investors in making their investment decision in an organization.

II. Ethics

Ethics are codes of conduct pooled by a community that draw a demarcation between moral and immoral or positive and negative. Ethics as defined by Merriam-Webster dictionary is the discipline that deals with what is good and bad and with moral duty and obligation (Merriam Webster, 2013).

A. Role of ethics in accounting

Ethics in accounting implies while conducting any sort of business affairs, accountants must act honestly and follow the morals and judgements. Ethics in accounting is crucial to follow due to the very nature of the accounting profession. Luca Pacioli, the "Father of Accounting", wrote on accounting ethics in his first book Summa de arithmetica, geometria, proportioni, et proportionalita, published in 1494. Ethical standards have since then been developed through government groups, professional organizations, and independent companies. These various groups have led accountants to follow several codes of ethics to perform their duties in a professional work environment.

Professional accountants and auditors must stick to the code of ethics, so that confidence and credibility retain in the accounting profession. There exist a set of guidelines issued by AICPA (American institute of certified public accountants), IIA (institute of internal auditors), IMA (institute of management accounts). Although it is difficult to verify whether accountants are following the code of ethics, all regulating bodies have an obligation to act as a watchdog so that firms adhere to the ethics. The nature of accountant's work puts them in a special position of trust and loyalty in relation to their clients, employers and general public, as they rely on their professional judgement and guidance in making their decisions. The accountants are relied upon because of their professional statues and ethical standards. To maintain trust, loyalty and to gain confidence of clients and the general public, accountants are required to follow certain ethical norms in business. Accounting being the backbone of any firm must go hand in hand with ethics, but unfortunately it has not. In the current scenario when the economic world

is witnessing a turbulent time, following ethics in accounting is a prerequisite. Ethical behaviour is necessary in the accounting profession to prevent any fraudulent activities or scams and to gain public trust in accounting profession.

B. Role of ethics in accounting comprises

1. Integrity

A professional accountant in performing his/her professional services must be honest and ethical. Accounting professionals must act fairly towards its stakeholders in the practice of their profession. Accountants shouldn't provide any false, misleading or deceptive information to its internal and external users.

2. Objectivity

A professional accountant should not allow bias, conflict of interest or undue influence of others to override professional or business judgements. He should be determined enough to be loyal towards his profession in any situation or pressure. A true accountant must oblige towards his moral responsibilities invariably.

3. Confidentiality

A professional accountant should respect the confidentiality of information acquired as a result of professional and business relationships and should not disclose any such information to third parties without proper authority unless there is a legal or professional right to disclose. It also should not be used for the personal advantage of the professional accountant or third party.

4. Responsibility towards Society

Accountants and auditors have the key responsibility to protect the interests of stakeholders and society. They should behave ethically with integrity and objectivity. Failure to do so leads to uncertainty in investors, shareholders and the work force in the organization.

5. Helps in retaining talented staff and in maintaining the goodwill of firm

Members of an organisation if act in accordance with the duties and responsibilities associated with the accounting profession and comply with ethical codes of conduct, it will not only enlighten the image of the profession and organisation but will also help to retain the talent in an organisation.

6. To attract customers and investors

Professional accountants are the key pillars in an organization. So to attract any third party, they must behave ethically and shouldn't provide any false feedback about firm's financial position and its profitability. Investors and public would not like to invest in such company which is not ethical towards his profession.

7. Professional Competence

Ethics in accounting ensures that the accountants maintain professional knowledge and skills at the level required to ensure that a client or employer receives competent professional service. A professional accountant should act with caution and in accordance with applicable technical and professional standards in providing professional services.

III. Research Methodology

The study here is primarily based on secondary data collected from relevant literature published in the journal, newspapers, websites, books, reports etc.

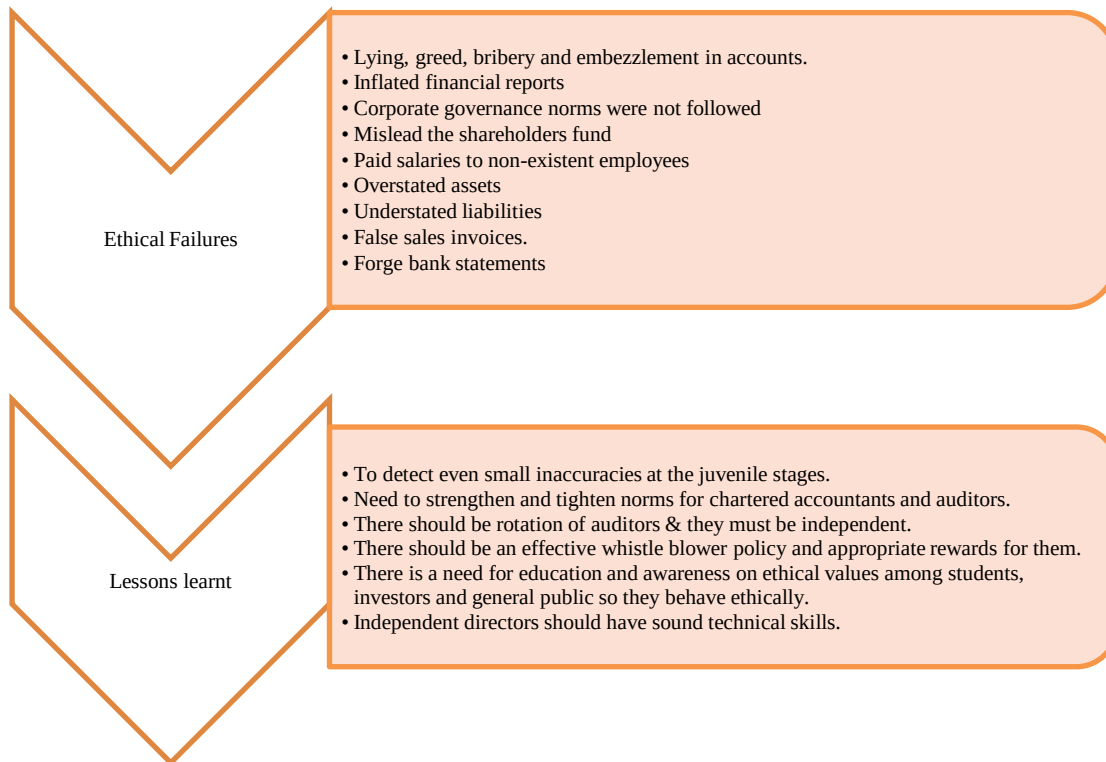
A. Case study on Satyam

Repeated incidences of creative accounting are a result of lack of ethical behaviour. One of ethical failure in accounting is evident from Satyam saga in India. Satyam scandal was completely a breakdown of trust and ethics. Satyam is the biggest accounting fraud in India's corporate history. It is also infamous as India's Enron. This scandal is a classic case of negligence of fiduciary duties, total collapse of ethical standards and a lack of corporate social responsibility. Greed for money, power, competition, success and prestige compelled Mr. Raju to violate all the duties imposed on them as fiduciary: the duty of care, the duty of loyalty, the duty of disclosure towards the stakeholders.

Satyam computer services limited established in 1987 by its chairman and promoter B Ramalinga Raju, and it was incorporated in 1991 as public limited company. Satyam's network covers 67 countries across six continents. In a 2000 SEC filing, Satyam Computer Services claimed to be the fourth largest provider of information technology services in India. In 2001, Satyam became world's first ISO 9001:2000 company to be certified 2 by BVQI. In 2003, Satyam started providing IT services to World Bank and signed up a long term contract with it. In 2005, Satyam was ranked 3rd in Corporate Governance Survey by Global Institutional Investors.

Ironically, the word ‘Satyam’ means ‘truth’ in Sanskrit language, but Raju’s admission accompanied by his resignation shows the company had been feeding investors, shareholders, clients and employees a steady diet of ‘asatya’ (or untruth), at least on its financial front. On January 7, 2009, Mr. Raju confessed in a letter to Satyam Computers Limited Board of Directors that “he had been manipulating the company’s accounting numbers for years”. Raju rationalized his deeds by stating, “It was like riding a tiger, not knowing how to get off without being eaten.” A week after Satyam founder B Ramalinga Raju’s scandalous confession, Satyam’s auditors Price Waterhouse finally admitted that its audit report was wrong as it was based on wrong financial statements provided by the Satyam’s management.

B. Ethical failures & lessons learnt from Satyam Saga



C. Need of strong corporate governance

Failure in corporate governance is a real threat to the future of every corporation. Accounting scandals not only drain the finances but also have damaged the accounting profession’s and country’s reputation. Intense competition and pressure of profit maximization forced companies to behave unethically. Despite India has so many anti-fraudulent laws like Prevention of corruption act, Prevention of Money Laundering, SEBI prohibition of fraudulent & Unfair Practices Regulations etc. there is still a need of effective corporate governance. Also there is a need to strengthen the existing corporate governance norms to prevent recurrence of such kind of frauds in future. The importance of good Corporate Governance has also been increasingly recognized for improving the firm’s competitiveness, better corporate performance, gaining investor’s faith and better relationship with all the stakeholders.

Effective corporate governance can be achieved by adopting a set of principles and best practices. This involves effective internal controls and effective independent scrutiny of the executive directors by non-executives. In particular, there are perhaps four main areas which a company ought to pay attention to in order to mitigate the risk of fraud: effective internal controls, the division of responsibility between chief executive and chairman, an audit committee and representation on the board of directors which are as under:

- **Effective Internal Controls:**

Internal controls include a control environment, risk assessment and management, monitoring and control activities. The presence of strong controls inhibits the possibility of financial malpractice. The collection of controls provides a key mechanism, combined with internal audit, whereby financial malpractice can be minimised.

- **Division of the Responsibility between Chief Executive and Chairman:**

One person being both chairman and chief executive is particularly dangerous. This is an essential division of authority in the board room. It prevents the unmitigated exercise of power by one person. Asil Nadir, for example, was CEO and chairman of Polly Peck.

- **Audit Committee:**

The audit committee is a relatively new development. It is responsible for supervising the auditors. It is important that the audit committee, to be effective, is independent; in particular, not staffed by friends, acquaintances or family members of existing executive directors. It also needs to meet frequently and to be staffed by experienced individuals.

- **Independent Board of Directors:**

To be effective, there needs to be strong & independent non-executive directors. As with the audit committee, the board of directors should not be friends, acquaintances or family members of existing executive directors.

IV. Conclusion

Enron scandal in US resulted in the passing of the Sarbanes-Oxley Act, 2002. Similar kinds of corporate governance reforms are needed in India too. Scandals have proved that there is an urgent need for good conduct based on reform and strong corporate governance, ethics and accounting & auditing standards. The Satyam scandal also highlights the importance of securities laws and corporate governance in the accounting sector. To prevent recurrence of similar frauds in future, Indian government should tighten the existing corporate governance norms and it is vital that all firms must conduct its businesses with keeping in mind the ethical framework.

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