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Should CPA Candidates Be Tested on Business Ethics?

Periodically, the American Institute of Certified Public Accountants (AICPA) validates the content and skill specifications for the uniform CPA examination by engaging subject matter experts, psychometricians, and data collection professionals to survey the opinions of practicing CPAs, a process that involves the input of many volunteer CPAs as well. The objective of this multistep procedure, called a practice analysis, is to

develop a set of knowledge, task, and skills statements that are reflective of the current workplace responsibilities of entry-level CPAs in public accounting and industry.

The importance of the resulting content specification outlines (CSOs) and skill specification outlines (SSOs) for a future CPA examination is heightened by the fact that the CSOs and SSOs are important drivers of the curricular decisions made by the accountancy departments and schools of many universities. In addition to alerting educators and students about what is necessary to pass the CPA exam, the CSOs and SSOs also facilitate consistent coverage of areas important to the public interest, thus providing support to

the use of the CPA exam as a prerequisite for licensure to practice public accounting.

The AICPA Board of Governors recently issued an exposure draft (ED) document, "Proposed Content and Skill Specifications for the Uniform CPA Examination," based on the most recent practice analysis. The ED reports that, as in the past, four separately scored examinations will cover auditing and attestation (AUD), financial accounting and reporting (FAR), regulation (REG), and business environment and concepts (BEC). The recommended change of most interest to those concerned about the ethics of accountants is that the coverage of the topics of professional and legal

responsibilities, including ethics, will expand dramatically. In the past, these responsibilities made up approximately 15%-20% of the REG exam. In the future, the REG exam will continue to cover legal liability and responsibilities and licensing systems, but only ethics rules covering taxation will be included. The topics of professional responsibilities, including ethics and independence, will be added to the AUD exam and comprise 16%-20% of the total.

We shouldn't be too overjoyed with this apparent recognition of how important applied ethics is for entry-level accountants. Public accounting owes its monopoly franchise and virtually entire existence to its responsibility to investors and the general public. Entry-level CPAs preparing financial information also require appropriate ability to apply ethical principles. Yet the CSOs and SSOs to be tested in the AUD exam appear to be entirely legalistic and based on rules only applicable to auditors. While independence is one of the more important characteristics of practicing public accounting ethically, it certainly isn't the only one, nor perhaps even the most important. It isn't relevant to finan-

cial information preparers. While the references cited in the ED include several concerning independence, there's no mention of textbooks or other sources of study regarding the principles of business ethics and how public accountants should apply them. The only textbooks cited as sources of examination content address auditing and attestation.

Interestingly, the U.S. Treasury's Advisory Committee on the Auditing Profession (Paulson Committee) has been meeting for some time. Its second draft report issued in July wears similar blinders that appear to limit the consideration of ethics to compliance with rules. It recommends professional examination content be regularly updated so it "reflects in a timely manner important...investor needs..." The report notes the importance of ethics: "ethical standards, fraud examination and forensic auditing, financial risk management, and valuation, and *subject matter relating to their application* [emphasis added] are an essential component of the accounting and auditing curricula and accordingly should be reflected in the professional examinations and throughout business and accounting coursework." Yet ethical standards are footnoted as consisting of only Public Company Accounting Oversight Board (PCAOB) Interim Ethics Standards. Missing is any reference to the work of the CFA Institute, the New York Stock Exchange Listing Rules that outline the importance of ethics codes, or acknowledgment of the importance of an ethical climate in an organization as required by the U.S. Sentencing Commission Guidelines.

Later in the report, the Paulson Committee addresses auditing firm fraud detection responsibilities. It

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recommends creation of a "national center to facilitate auditing firms' and other market participants' sharing of fraud prevention and detection experiences, practices, and data and innovation in fraud prevention and detection methodologies and technologies, and commission research and other fact-finding regarding fraud prevention and detection. Further, it recommends the development of best practices regarding fraud prevention and detection." This seems to be an unnecessary duplication of effort, as the Institute of Internal Auditors (IIA), the Association of Certified Fraud Examiners (ACFE), and the AICPA just recently announced the release of fraud guidance titled "Managing the Business Risk of Fraud: A Practical Guide."

The earlier draft of the Paulson Committee report also recommended "clarification" by the PCAOB and Securities & Exchange Commission (SEC) of the auditor's (limited) role in detecting fraud and publicity about that limited role to lower public expectations and reduce the "expectation gap." The comment that the public believes auditors can detect more fraud than the auditors believe themselves drew a large number of adverse comments and was removed from the July report.

In the AUD portion of the AICPA's exposure draft, the only mention of fraud is under risk assessment: "Assess the risk of material misstatements from errors, fraud, and illegal acts by clients" and "Consider fraud risks." There's no mention of fraud prevention or the importance of an ethical culture in the organization to minimize fraud risks. The same section does note under internal control that the first SSO listed is "Perform procedures to assess the control environment in accordance with the COSO framework." There is no indication that application of the basic principles of integrity and ethical values underlying COSO will be tested.

In contrast with the CPA examination, one of the CSOs being tested in the examination for the Certified Management Accountant (CMA®) designation is "Evaluation and resolution of ethical issues, such as fraudulent financial reporting." The Candidate Body of Knowledge required for passing the Chartered Financial Analyst (CFA) examination includes Ethical Practices as well as Professional Standards of Practice.

KPMG's recent announcement that it is adopting an enhanced global code of conduct highlights the fact that all of the Big 4 firms expect their

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partners and staff to live up to far more stringent requirements than the legalistic rules tested by the CPA examination. As noted in last month's column, however, only half of the respondents to a poll of MBAs think their personal integrity figures largely in corporate recruiters' evaluation of them as potential employees.

A study of each Big 4 firm's code of conduct reveals both common and differing threads. Some are long and very comprehensive, and others are shorter. Each firm expects behavior that conforms to a set of values or ethical principles, but the values are different in each firm:

◆ *Firm A:* Guiding Principles are: We lead by example. We work together. We respect the individual. We seek the facts and provide insight. We are open and honest in our communication. We are committed to our communities. Above all, we act with integrity.

◆ *Firm B:* We are: People who demonstrate integrity, respect, and teaming; People with energy, enthusiasm, and courage to lead; People who build relationships based on doing the right thing.

◆ *Firm C:* Integrity, Outstanding value to markets and clients, Commitment to each other, Strength from cultural diversity. Ethical Principles are: Honesty and Integrity, Professional Behavior, Competence, Objectivity, Confidentiality, Fair Business Practice, Responsibility to Society, Respect and Fair Treatment, Accountability, and Decision Making.

◆ *Firm D:* Achieve Excellence, Develop Teamwork, Inspire Leadership.

Three of the four firms mention help or hotlines in their codes. Two firms promise no retaliation for those who speak up to report

wrongdoing.

Perhaps it's time to start thinking less that a major purpose of the uniform CPA examination should be to weed out people who have difficulty with the intricacies of the latest FASB pronouncement. Instead, the CPA examination could be useful as a screen to help distinguish those individuals capable of accomplishing the major purpose of public accounting and singular reason for its existence. That is, serving the public interest by performing ethically driven audits! It would also help identify ethical preparers of financial information, who have no less need to apply ethical principles in their decision making. Testing one's ability to remember rules applicable only to auditors will never achieve these valuable goals.

Audits need to obtain independent support for even the most complicated collateralized debt obligation assets that might not even show on the balance sheet. It should be unethical for an auditor to just accept the value of a mortgage security that's only an estimate determined by computer software using assumptions provided by the client. This was one aspect of Andersen's flawed audit of Enron.

As Yogi Berra said, "It's déjà vu all over again!" ■

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