Business Horizons (2015) **58**, 485—492

Available online at www.sciencedirect.com

ScienceDirect

KELLEY SCHOOL OF BUSINESS

INDIANA UNIVERSITY

www.elsevier.com/locate/bushor

Between a rock and a hard place: Conflict minerals and professional integrity

Kate Jelinek

College of Business, University of Rhode Island, Ballentine Hall, 7 Lippitt Road, Kingston, RI 02881, U.S.A.

KEYWORDS
Auditing;
Auditor integrity;
Auditor lobbying;
Conflict minerals;
Dodd-Frank

Abstract Against the backdrop of integrity as put forth in the American Institute of CPAs' (AICPA) Code of Conduct, this article takes a close look at a section of the 2010 Wall Street Consumer Protection Act, commonly known as Dodd-Frank. Interestingly, Section 1502 of the Act contains a provision that puts forth new reporting and disclosure requirements for publicly traded companies that manufacture products consisting of 'conflict minerals' derived from the violence-ridden Congo region. Though the provision is unlikely to stop the violence, the cost of disclosure for publicly traded companies is frighteningly high. This article examines the Big 4 accounting firms' lobbying efforts that preceded passage of the Act and asks whether it is coincidental that Big 4 firms stand to gain from the Act's passage, as Section 1502 provides a new revenue stream that could potentially reach into the billions. This article also includes an examination of the origins of auditing, a very brief history of auditing in the U.S., and a look at the accounting industry's lobbying efforts in recent years. The article concludes with suggestions for the profession, firms, and individual auditors.
© 2015 Kelley School of Business, Indiana University. Published by Elsevier Inc. All rights reserved.

1. The auditing profession: What a change a century can make

> *The origin of auditing goes back to times scarcely less remote than that of accounting. . . . Whenever the advance of civilization brought about the necessity of one man being entrusted to some extent with the property of another the advisability of some kind of check upon the fidelity of the former would become apparent.* (Brown, 1905, p. 75)

The auditing profession has a rich history steeped in the strong moral character and values necessary to carry out such an important function. Existing since ancient times, auditing is still among the most critical corporate governance mechanisms for protecting shareholders and providing proper information disclosure. It plays a unique and vital role in our society, supporting the efficiency and effectiveness of our capital markets system. As noted by Chief Justice Warren Burger in *United States v. Arthur Young & Co. et al.* (1984), the auditor's special role must be supported by a special character:

> By certifying the public reports that collectively depict a corporation's financial status, the

E-mail address: kjelinek@uri.edu

0007-6813/$ — see front matter © 2015 Kelley School of Business, Indiana University. Published by Elsevier Inc. All rights reserved.
http://dx.doi.org/10.1016/j.bushor.2015.05.001

> independent auditor assumes a public responsibility transcending any employment relationship with the client. The independent public accountant performing this special function owes ultimate allegiance to the corporation's creditors and stockholders, as well as to the investing public. This "public watchdog" function demands. . .complete fidelity to the public trust.

Arthur Andersen, founder of the namesake firm, exemplified that character described by Chief Justice Burger. During the early days of the auditing profession in the United States, Andersen was known as an auditor's auditor; his motto was "think straight, talk straight" (Knapp, 2013, p. 4). A legendary story about the young Andersen describes a particular interaction with a client in 1914. Apparently, the client—a local railroad—pressured Andersen to approve questionable transactions that purposely understated expenses and therefore falsely boosted earnings. Despite the fact that the young Andersen was worried about making payroll at his own company, he stood up to the client, saying there was "not enough money in the city of Chicago" to make him approve the numbers (Brown & Dugan, 2002).

Fast forward a century from Andersen's bold declaration that he would not place profits ahead of principles and things seem quite different. The Big 4 accounting firms—the group of large organizations remaining since the demise of Andersen's firm—"completely dominate the industry" (big4accountingfirms.org). Together, Deloitte, PricewaterhouseCoopers (PwC), Ernst & Young (EY), and KPMG audit more than 80% of U.S. public companies. The perception is that these four firms uphold standards set by the American Institute of CPA's (AICPA) Code of Conduct, which is a collection of statements outlining a CPA's ethical and professional responsibilities. However, as will be detailed here, the Big 4 firms have assembled a political lobbying machine that increasingly appears as though its primary aim is to create new business opportunities. Given the clarity of the code—"Service and the public trust should not be subordinated to personal gain and advantage" (AICPA, 2014)—it is worth questioning if these firms' commitment to this code is what it should be.

Against the backdrop of integrity as put forth in the AICPA's code, this article takes a close look at a section of the Dodd-Frank Wall Street Reform and Consumer Protection Act, commonly known as Dodd-Frank, passed in 2010. Interestingly, Section 1502 of the Act contains a provision that puts forth new reporting and disclosure requirements for publicly traded companies that manufacture products consisting of 'conflict minerals' potentially derived from the violence-ridden Congo region. These include gold and, among other substances, the 'three Ts': tungsten, tin, and tantalum. Companies whose production processes might somehow involve the use of these materials now have to report to the SEC whether or not their particular materials originated in the Democratic Republic of Congo or an adjoining country and, if they did, what the company did to oversee the handling of these materials from the point of origin forward. Regardless of one's thoughts on the merits of such regulation, it is worth wondering what this provision is doing in a congressional bill supposedly intended to crack down on corrupt lending and investing practices at too-big-to-fail financial institutions.

Section 1502 may seemingly be motivated by a concern that the sale of such minerals could be funding violence. However, given that the new reporting requirement covers substances that are widely used across many industries in everything from smartphones to jewelry, numerous companies will be required to comply, and parties involved in overseeing compliance will be presented with a considerable new revenue stream. Now consider that in 2008 during the run up to the 2010 passage of the Dodd-Frank legislation that included this conflict minerals provision, significant Big 4 political donations were directed toward Christopher Dodd, then-U.S. Senator from Connecticut and co-author of the law. While the law's passage represented a significant business opportunity for Big 4 firms, a Tulane University study commissioned by Senator Dick Durbin of Illinois found that the costs of implementing Section 1502 would be frighteningly high. This study estimated that the cost could reach $7.93 billion, more than 100 times the cost originally estimated by the SEC. So, while Big 4 firms stand to gain, most companies stand to lose. Moreover, research indicates that Section 1502 is unlikely to stop violence in the region and could even make things worse (Seay, 2012).

Very pointedly: If the accounting profession endeavors to lobby lawmakers to craft laws that create more business for the industry at the expense of the public—who works for publicly owned companies, owns stock in or buys products from those companies, and/or works for other companies doing business with these publicly owned companies—is the profession remaining faithful to its oath of integrity?

In this article, we first consider the origins and purpose of auditing and briefly review the history of the profession in the United States. Next, we examine the AICPA's statement on integrity and the profession's commitment to the public trust, and we

Download English Version:

https://daneshyari.com/en/article/1013874

Download Persian Version:

https://daneshyari.com/article/1013874

Daneshyari.com