THE SMALL BUSINESS INSTITUTE® CONSULTING TEAM’S

ETHICAL DILEMMA

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ABSTRACT

Professor Hucklebee did not know how to respond when his SBI® consulting team informed him that their client admitted to cheating on his Federal and state income taxes. The client specifically said “I cheat on my taxes.” The semester long class was scheduled to end the following day with the team’s final public presentation. The team presentation was a large portion of each student’s overall grade. Up to this point, all other requirements for the course were complete, including the written report.

All students were required to do an oral presentation because the professor believed that it met Bloom’s highest level of learning—defense of one’s recommendations. Answering questions from other faculty members, other students, and outside members in the public make the presentation and defense more realistic.

If the Professor excuses one or more team members from the presentation requirement, he would violate other students’ distributive justice— that all students be treated equally. If he forces the consulting team to present, he might violate individual moral codes. If the students tell the truth about their client in public are there any liability issues? What should the professor do?

This case could be used in any class that covers ethics by first asking which groups cheat more on their taxes: young versus old, poor versus rich, or men versus women. The discussion can then evolve into small business ethics and the impact of cheating on the value of any small business.

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Background

As Dr. Hucklebee sat and listened to his student team he was not sure how to respond. After hearing two team members talk at once, he asked them to stop, take a breath, think back, and tell him exactly what their small business client said.

Although they stated the encounter in slightly different words, both members collaborated each other’s version - their small business client blatantly admitted that he was cheating on his federal and state income taxes (Appendix 1).

The students had almost finished a semester course on consulting with a small business client/owner. The course was a senior level class requiring students to determine the client’s problems, develop alternatives, and recommend solutions. The last assignment was to orally
present their report to the client, business faculty, and public. The students’ grades depended on completion of all assignments including the written report, the oral report, and an assessment by the small business client. This was a capstone course and mandatory for the students to graduate.

**The Small Business Consulting Class**

The Small Business Consulting Class was part of the University and College of Business’s small business and entrepreneurship program. The class was part of a three course sequence. These classes were: fundamentals of entrepreneurship, new venture planning, and the consulting class. Many of the students had completed all three courses and were using the classes to gain necessary knowledge to start their own business.

The University belonged to the Small Business Institute®[^1] that was a national organization of schools dedicated to field based learning. The professor had been part of this national organization 20+ years and had never had an incident like this occur.

The instructor found small business clients for the course from the local Small Business Development Center, the Chamber of Commerce, and the professor’s contacts. The professor had personally used this client’s business many times, made friends with the owner, told the owner about the class, and received the owner’s request to be a client.

Professor Huckelbee stated that the benefits to students were fourfold. The field based learning gave students a real world business in which to apply what they had learned. The students highlighted the class on their resumes and discovered that most recruiters asked about the experience. Several reported that it made them more comfortable going into interviews with the belief that they had something to offer their potential employers. Lastly, the course required the participants to not only use what they had learned but made them integrate all the areas of business from accounting, management, finance, strategy etc into the final recommendations. As a result of these “real world experiences” both student expectations and evaluations of the course were high.

**Program and Course Requirements**

All the clients were interviewed, screened by the instructor, and told the requirements of the class. The instructor required that all the small business clients/owners participating in the program meet the following requirements: 1) they had to be in business for more than two years, 2) they had to meet with the students weekly, 3) provide enough information for the students to review, and 4) attend the oral report on campus. The client was personally asked by the professor if he wanted the students to review his business’ financials. The provision of financial statements was not required for the clients to enter the program. Some clients agreed and some did not. This client wanted to provide his financial statements because he wanted the team to determine the business’ value for a possible future sale.

[^1]: The Small Business Institute® is a national organization and the name is trademarked.
The students were assigned to teams by the instructor to ensure that each team had marketing, management, finance, accounting and other expertise needed for the analysis of the client’s situation. This team had one finance/accounting student, one marketing student and one management student. Each student had to sign a letter agreeing to maintain confidentiality of all the client’s information. In exchange, the client signed a waiver forfeiting their right to sue based on any of the team’s analysis, findings, or recommendations. The waiver included the students, university, and professor.

The course required the students to establish rapport with the client, meet the client once a week, determine the business’ major issues, develop alternative solutions to these issues, and recommend solutions. The team’s written report had been graded, edited, and rewritten several times. It had been copied and bound with one color copy for the client. Tomorrow the team needed to orally present their report to the class, the instructor, the client, and public visitors.

The course was structured so that successive course requirements moved up Bloom’s learning taxonomy to the highest level (Bloom’s Taxonomy is in Appendix 2). At the lowest levels the students had to recall material from their accounting, finance, management, marketing, and other classes. Then they had to identify the clients’ major business issues (Level 2). Once identified the team had to analyze the issues, determine alternatives, and determine the pros and cons of those alternatives (Level 4). They had to compose solutions to those issues that fit together and integrate finance, accounting, and marketing issues (Level 5). Then the students were required to orally defend their recommendations (top Level 6) and answer questions by the instructor, other class members, the client, and university guests. This oral presentation was worth two fifths of the final grade and was mandatory and necessary to pass the class.

The high number of points reflected the difficulty and Bloom’s Level 6. Not only did the team have to organize and complete an oral presentation they had to defend their analysis and recommendations. The requirement to face probing questions from unknown members of the public made the assignment more difficult, challenging, and worth more points than any other assignment. The instructor had on many past occasions resolutely refused to let the students present their conclusions to just him or the client and the professor.

**The Dilemma**

Once the team caught their breath, the professor asked them to repeat the small business client’s exact words which were “I cheat (on my federal and state taxes).” The client further stated that he included personal expenses on his business’s financial statements and regularly removed cash from the cash register. This inside knowledge created problems for the following individuals: the students, the client, the professor, the university, and the public visitors.

**The Students Perspectives**

Each of the students had a different perspective. The finance/accounting student was the most upset and was close to refusing to work with the client. He would do the oral report only if the
Professor “absolutely required him to do it.” The management student was the least upset and was motivated to finish the class so he could graduate. The marketing student was marginally concerned.

The Professor’s Perspective

The professor was concerned about liability because the oral presentation was open to the public. The professor had invited other faculty, the School of Business Dean, alumni, and SCORE (Service Core of Retired Executives). SCORE members are retired business professionals who dedicate their time and advice to small businesses in the local community.

Should Professor Hucklebee require the team to finish the project by giving the oral presentation to the client and public tomorrow? If the purpose of the class was to provide “real world experiences” was not being exposed to “real world warts” part of the experience? If the team did not finish the oral report how would that be equitable to the other five student teams who had to do an oral report, defend their solutions, and answer tough questions from the public? How would this team fulfill the requirements for the class? What were the ethical and legal ramifications of any option? Did the confidentially statement apply? Should there be concern about the oral presentation being open to the public? What action should the professor take? Should the accounting/finance student who was the most upset inform the IRS? Is cheating on income taxes so rampant the students, the professor and the University should ignore it?

Appendix 1

Written Statement from the Accounting and Finance Student Team Member to the University President

On November 28 I and Sam McClure met with our client at the Old Chicago’s restaurant at approximately 6:20 pm for the purpose of engaging in conversation related to the small business counseling class assignment. The conversation began with a discussion of the financial condition of the firm for the purpose of valuing the business (per the request of the client). I stated, “in order to increase the value of the business you must lower your expenses.” To this, the client replied, “I cheat.” The conversation continued about the financial condition of his business, and he declared that there were all sorts of different expenses in there, including his car payment and others. Later in the discussion, the client stated that “I am fully vested in social security, therefore I never plan to pay social security tax again.” He also stated that he has not paid social security tax in the past few years. Furthermore, the client declared, “I run a cash business and who’s going to know if I take cash out of the register.” After this point in the
conversation, the client’s daughter (whose name I do not know) arrived, and the conversation shifted to a more social subject matter, and at approximately 7:30 pm we ended the conversation and parted ways. My desire to terminate all business relations with this client is based on the personal belief that the business conduct of this client was unethical and I do not feel comfortable making any professional recommendations to the client.

Sincerely,

James VanArasdale, Sam McClure, and Sally Henderson

*The names of the students, client, University and city were disguised or removed. The client’s reference to social security is not completely clear – possibly he was upset about the amount of social security taxes he was paying.

Appendix 2
Bloom’s Taxonomy

Bloom’s Levels- lowest to highest:

Knowledge: arrange, define, duplicate, label, list, memorize, name, order, recognize, related, recall, repeat, reproduce state.

Comprehension: classify, describe, discuss, explain, express, identify, indicate, locate, recognize report, restate, review, select, and translate.

Application: apply, choose, demonstrate, dramatize, employ, illustrate, interpret, operate, practice, schedule, sketch, solve, use, write.

Analysis: analyze, appraise, calculate, categorize, compare, contrast, criticize, differentiate, discriminate, distinguish, examine, experiment, question, and test.

Synthesis: arrange, assemble, collect, compose, construct, create, design, develop formulate, manage, organize, plan, prepare, propose, set up, write.

Evaluation: appraise, argue, assess, attach, choose, compare, defend, estimate, judge, predict, rate, core, select, support, value, evaluate.

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Critical Incident Synopsis

The Student Consulting Team’s Dilemma presented a real world ethical issue. The team’s small business client blatantly informed them that his financial records were not accurate. He admitted including non-business related expenses in his Federal and state income taxes to minimize tax payments. The semester course was almost completed with the written report ready for the client. The last remaining course requirement was to orally present and most importantly defend the report to the client, the class, the instructor, and university guests.

To complicate the issue the accounting/finance student would perform the oral report only if “absolutely required by the instructor.” The remaining two students looked to the instructor for guidance.

Learning Objectives

The ethical case can be used in any number of courses such as management, strategy, entrepreneurship, small business, or other disciplines. The short case presented an ethical dilemma with which students and professors can identify. What do they do now that is ethical and equitable to the team, the client, and the other students? How do you change the grading scheme at the last minute and make it equitable to everyone?

In addition, the dilemma could be used in any entrepreneurial or small business class. The case raises ethical issues that all small business owners/managers face. Especially poignant is that cheating affects the selling price of the business. After discussing questions 1-7, ask what this business is worth. Let the students experiment what the business is worth if the owner only showed a breakeven on their taxes, a $70,000 profit, or a $90,000 profit. The new owner told Professor Hucklebee that she was able to buy the business for a “smidgen” – basically nothing. Then ask the question if the owner wanted to sell this business for $100,000 and got very little was his cheating worth it based on strictly a financial or economic analysis?

The authors have had good success by starting the class with the first discussion question-which groups are more likely to cheat: young versus the elderly, rich versus the poor versus the middle class, or men versus women. Then present the answers to question 1 and ask them why these groups are more likely to cheat. This teases out some good explanations by the students. After engaging their interest, begin with the other discussion questions.
The students should be able to:

1. Identify the ethical issues on the part of the client, the team and the instructor (Level 1).
2. Identify some alternatives for the instructor (Level 2).
3. Analyze the ethical and equitable results of those alternatives (Level 3).
4. Synthesize and apply a result that meets competing ethical objectives for the team, the other students, the instructor, and the client (Level 4).

Discussion Questions

1. According to the IRS, tax fraud cost the U.S. $113 billion in 1991. Some groups cheat more than others. Ask the class which group they think cheat the most: rich versus the poor versus the middle class, young versus the elderly, service corporations versus manufacturing etc.
2. Does that fact that many corporations and individuals cheat on their income taxes exonerate the client?
3. What is the dilemma in the critical incident?
4. How should the instructor deal with the following: 1) the client, 2) the students, and 3) protect the university?
5. If one student leaves the group due to moral self-obligation how will it affect the rest of the group? How will it affect the grades? What is equitable for the rest of the group and for the rest of the class?
6. Does the fact that the professor would never let previous or current students miss the oral presentation to the public complicate the situation? What are some alternatives and their pros and cons?
7. Discuss the implications of each decision the team has made and will make.
8. For small business or entrepreneurial classes, the question is what is this business worth if the owner reports no net profit?

Answers to the Discussion Questions

1. Does that fact that many corporations and individuals cheat on their income taxes exonerate the client?
The figure of $113 billion in 1991 is very large and as one author pointed out would cover the U.S. deficit in 3-4 years. No they are not exonerated.

2. Does that fact that many corporations and individuals cheat on their income taxes exonerate the client?
   - According to the IRS, tax fraud cost the U.S. $113 billion in 1991. Some groups cheat more than others (Smith, 1991). Ask the class which groups they think cheat the most: rich versus the poor, young versus the elderly, service corporations versus manufacturing etc. A *Money* poll in January 1991 found that the public voted the following as the most likely to cheat: men regardless of income (52%), and the young (50%). Those voted the least likely: the elderly (71%), the poor (61%) and women (56%) (Smith, 1991).
   - Smith (1991) found that there is a surprising amount of underreporting by the poor and elderly. The former live on cash revenues and can understate it. Many elderly use cash to underreport because they are on fixed incomes. Both the rich and the poor are the most active under-reporters.
   - Individuals and organizations in the service industry under-report up to 84% of their tips. The author concludes that those groups that are the least likely to get caught do the most thus the service workers and those individuals and organizations dealing in cash. The article also reports that men are much more likely than women to report incorrectly.
   - The least likely to cheat are those wage earners whose wages are reported by their employers. Also the middle income taxpayers are the least likely (Smith, 1991).

3. What is the ethical dilemma in the critical incident? Students may identify a number of dilemmas facing the participants in the case.

   - *The professor* faces the primary dilemma and must decide whether to continue with the class presentations and embarrass the business owner in front of the review group including business leaders who may know the client. His dilemma is compounded by having to decide whether to confront the client or ignore the client’s comments. He also must decide how to grade the accounting/finance student without violating distributive justice by treating him differently from the other students. Conversely if he forces the student to present in front of the client he violates the student’s moral rights - the student’s conscience.
   - *The students* involved in the project face the ethical dilemma of going against their ethical principles by continuing the presentation disclosing the client’s statement. Do they delete the statement from the presentation or fail to inform the IRS? The marketing and management students’ dilemma is the desire to get a grade and finish their education versus standing on principle and creating dissension within the group.
The accounting finance student is the most upset. Why? Accountants are held to ethical obligations and a CPA must comply with the Code of Professional Conduct. Accountants must take an ethics course offered by the Accounting Society before he/she can become a licensed CPA. Although the student is majoring in accounting is he/she obliged to adhere to the Professional Code of Conduct since he/she is not a CPA? The Professional Code provides guidance to the conduct of the professional when preparing accounting reports/tax returns for clients but does not provide guidance about actions to take when a client acts in an unethical manner. It is not unusual for small business owners to have a company car. For example, the owner’s car may be listed in the name of the company and the company makes the car payments and insurance payments. Does the student really have full information to make a judgment? Many individuals may say they “cheat” on a tax return, yet are conforming to tax codes- many parts of the tax code are open to interpretation and there have been reported instances of IRS employees not being consistent when providing advice to taxpayers.

Does an accountant or professional tax prepare the business owner’s taxes? If so, then it should be assumed that the tax forms were prepared appropriately.

It is stated clearly in the syllabus that all students must participate. At most universities a syllabus is considered a contract. Should the professor change the course requirements at the end of the semester? Is the issue such that inequitable treatment of students can be supported (specifically requiring all other students to make an oral presentation)?

Is there any legal contract between the students/professor and the business client? Each entered into a verbal agreement to provide something. Students signed a confidentiality agreement and the business owners signed a waiver.

4. How should the instructor deal with the following: 1) the client, 2) the students, and 3) protect the university?

- **The client:** Since the professor knows the client personally, he must decide whether to tactfully inform the client of the awkward situation and suggest the student project be terminated while leaving it up to the client to “right his wrong” actions. Since he is only dealing with “hearsay” from the students, he may also caution the client about possible repercussions if any of the students forward his comments to other authorities. At any rate, the professor has to contact the client and hear the client’s story. In this critical incident, the professor only has information provided by the students.

- **The students:** The professor has heard the students’ story of what happened. Is there more information he needs? Without any other information, the professor should not coerce the students to take any action deemed unethical. He should have a discussion with the students and entertain their recommendations and evaluation of the alternatives. He could bring in the University’s legal counsel to
advise them of potential courses of action and the ramifications. Those students who vehemently oppose any further contact with the client should be given an optional or supplemental assignment for grade purposes. This student’s grade could also be based on his work to the present. Those who want to finish the assignment could give their presentation but without the outside business people or the client present. The instructor should discuss the incident with the entire class so all would know why the separate grading took place.

- **The university:** The professor should contact the Dean and the University attorney to obtain their input. At a minimum the professor could protect the university by not having the team present to the client especially with the public present. This action would create a legal liability for alleged libel by the students, the professor, and the university.

5. If one student leaves the group due to moral self-obligation how will it affect the rest of the group? How will it affect the grades? What is equitable for the rest of the group and for the rest of the class?
   - Should one student’s concerns about a client’s behavior be more important than equitable treatment for all the students? To void the syllabus is to void a contract between the student and the University.
   - Does one student have the right to judge the client especially if it is detrimental to the group and to the class?
   - The rest of the consulting team should not be adversely affected by the loss of a member. Those remaining in the group can certainly complete the preparation for the presentation. At worse the group will have a topic for discussion in developing their own ethical values.

6. Does the fact that the professor has never let any students miss the oral presentation to the public complicate the issue? What are some alternatives and their pros and cons?
   - The professor calls the client and terminates the consulting agreement.
     - Pro—it keeps the students, professor and University from public embarrassment
     - Pro-it signals to the client that the behavior is unacceptable
     - Con-it violates distributive justice because the other students have to face public questions.
   - The professor forces the team to present to the client and public.
     - Pro-the team faces the same grading scale as the other students
     - Pro-most of the team just want to finish the class and graduate.
     - Con-it is forcing one student to go against his morals which would violate his moral rights.
   - The professor leaves out the accounting student and has the rest of the team present to the public and the client.
- Pro- the other team members can finish and graduate.
- Pro- the professor can give the accounting finance student the grade he has earned to date.
- Con – the accounting student is not held to the same standards as the rest of the class. This violates the other students’ distributive and procedural justice.

- The professor can relent and let the students present the case to just him.
  - Pro- it keeps the students, the university and the client out of public disclosure.
  - Pro- it allows the students to finish the class
  - Con- it is violates the other students’ distributive justice – all students are not treated fairly.

- The professor should do one of the above and notify the IRS.
  - Pro- a tax cheater is exposed.
  - Con- the professor is only relying on the students’ word and this is hearsay.

- The accounting/finance student should notify the IRS.
  - Pro- it is in keeping with his moral structure.
  - Pro- he is close to graduating and close to being held to accounting standards.
  - Con- it could involve him in discussions with the IRS.

7. There are three possible ways to value a business: 1) net asset value, the value of comparable businesses, and some form of financial performance based on earnings or net profitability.
   - Net asset value. The potential buyer found out from the landlord that the lease was expiring. The tenant had installed tubs and plumbing what were single use items. Since the lease was expiring the potential buyer asked the landlord to leave the fixtures in place because she wanted to take over. Thus the value of the fixed assets was essentially zero. (The seller would have to remove them and leave holes in the walls so the landlord was eager to not have them removed.)
   - To determine value for a residential house, appraisers use a composite or average of comparable houses in the neighbor. There were no businesses providing this service with 30 miles so comparables did not exist.
   - One method the authors use is to approach the value of the business from the viewpoint of the potential buyer. This method attempts to put a value
on the intangibles or good will. The method takes the time it would take for
the potential owner to build a comparable business from scratch in years.
This is used as the “multiplier.” The amount the buyer could earn from
investing their down payment in some other investment is added to a
comparable salary that they could earn if they did not do this business- they
left a job making $30,000 to pursue this business plus they would “lose” the
opportunity to earn $3,000 from investing their down payment in some
other investment.

Start with the following assumptions:
The value of the assets is essentially zero
The new buyer thinks that they could build a comparable business from scratch
in three years so 3 is the “multiplier.”
Assume that if the seller had been honest the net profit should have been
$70,000 or $90,000
The buyer will have to leave a “safe” corporate job making $30,000 a year.
The buyer would forfeit making $3,000 interest on some other investment.

<table>
<thead>
<tr>
<th>No</th>
<th>Item</th>
<th>Zero Net profit</th>
<th>$70,000 net profit</th>
<th>$90,000 net profit</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Adjusted value of tangible net worth</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>2</td>
<td>Buyer’s potential earnings if the down payment was invested in safe or other investment</td>
<td>3,000</td>
<td>3,000</td>
<td>3,000</td>
</tr>
<tr>
<td>3</td>
<td>Reasonable salary for owner</td>
<td>30,000</td>
<td>30,000</td>
<td>30,000</td>
</tr>
<tr>
<td>4</td>
<td>Average annual net earnings of the business for the past 5 years</td>
<td>0</td>
<td>70,000</td>
<td>90,000</td>
</tr>
<tr>
<td>5</td>
<td>Extra earning power of potential business over salary lost to buyer and profit from not investing down payment in some other investment: Line 4-line2-line 3</td>
<td>-33,000</td>
<td>37,000</td>
<td>57,000</td>
</tr>
<tr>
<td>6</td>
<td>Value of the intangibles Multiplier of 3 times line 5</td>
<td>-99,000</td>
<td>111,000</td>
<td>$171,000</td>
</tr>
<tr>
<td>7</td>
<td>Final offer price</td>
<td>0</td>
<td>111,000</td>
<td>$171,000</td>
</tr>
</tbody>
</table>
The conclusion is that if the owner had been honest and not cheating on his taxes, the business value would have been $111,000 if $70,000 net profit had been reported or $171,000 if $90,000 net profit had been reported. The conclusion is that buyers, bankers, or other investors will value a business less when the seller under reports net income.

Research

The material for this critical incident was collected by interviewing the instructor and subsequent interviews to determine accuracy.

Relevant Literature


See also:


Epilogue

The instructor turned the dilemma into a teaching situation and asked the students what the options were and their ethical pros and cons. When the accounting/finance student became more emphatic that he would not do the oral report, the instructor asked him for an equitable alternative that would fulfill the oral requirement. It was pointed out that the other teams had this requirement.
After some discussion the students asked the instructor to “fire” the client and take the client’s place for the oral report. The instructor always attended and therefore agreed to act like the “client”.

The instructor called the client, confronted him with his statement, and informed him that the program was terminating his case. The client became livid, displayed a colorful and thorough grasp of foul language, and hung up.

The instructor immediately informed the Dean of the College of Business who concurred with the conclusion. The instructor suggested to the Dean that he brief the University President upon the remote possibility the client would escalate the issue. Upon arriving at the President’s office and before he could say anything both the President and the Vice President for Academic Affairs immediately questioned the Dean about the incident- the client had called both their offices to complain. The instructor and the Dean fully briefed the President who concurred with the conclusion. Having been legally trained, the President was certain that the university would prevail in any lawsuit.

When the client called the Dean, the Dean told him that he agreed with the termination, he had the support of the President and Vice President for Academic Affairs, and that if the client wished to pursue the situation he would have to do so legally. A university lawyer remarked that the client would have been “crazy” to sue because he would have to admit in court that he cheated on his taxes. Fortunately, the client did not pursue the matter further and within a year sold the business.

The instructor was told by the university attorney to not call the IRS because he would be engaging in hearsay. Only the students who heard the comment would have standing in court. The accounting/finance student threatened to call the IRS but the professor was not aware if that happened. The instructor now goes back to the business which is under new ownership.

The client tried to sell his business for $100,000 but his financials indicated that the firm was not making any profit. The potential buyer called the landlord who leased the space to the client and found that the lease was expiring. The potential buyer then suggested that the landlord not remove any of the equipment (mostly fixed plumbing) and furnishings and they would take them over. When the seller called the buyer, the buyer informed him that he knew his lease was expiring and the buyer could obtain all of the furnishings and equipment for nothing. After exploding and yelling at the buyer, the seller hung up. Subsequently the seller called back in two days and accepted a “minimal” (smidgen in the owner’s words) payment for the business.

Appendix 1  Overview of Ethics and the Importance of Ethics

Business ethics comprises the principles and standards that guide behavior in the world of business. Investors, employees, customers, interests groups, the legal system, and the
community determine whether a specific action is right or wrong, ethical or unethical. The judgments of these groups influence society’s acceptance or rejection of a business and its activities. Accounting fraud, such as that presented by the key issue in the client’s statement about cheating on taxes, is evidence of declining ethical standards in business, a clear indication of how a business can be rejected by relevant stakeholders. Professionals in any field—just like the students and professor in this case—must deal with individuals’ personal moral dilemmas because these issues affect everyone’s ability to function on the job. It is important to recognize the relationship between legal and ethical decisions. By studying business ethics, a student will begin to understand how to cope with conflicts between personal values and those of the organization with which the student works.

The case of the ethical dilemma with this client would allow the team to extrapolate to a larger scenario and offer an opportunity to review the progression of the study of business ethics, particularly the institutionalization of business ethics in the 1990s when the Federal Sentencing Guidelines for Organizations (FSGO) was approved by Congress in November of 1991 and with the passage of the Sarbanes-Oxley Act (SOX) in 2002. The FSGO set the tone for organizational ethical compliance programs in the 1990s; the Guidelines codified into law incentives to reward organizations for taking action to prevent misconduct such as developing effective internal legal and ethical compliance programs and providing provisions to mitigate penalties for businesses that strive to root out misconduct and establish high ethical and legal standards.

Likewise, if a company lacks an effective ethical compliance program and its employees violate the law (such as the case client), it will incur penalties. The FSGO establishes the approach that by taking preventive action against misconduct, a company can avoid penalties if a violation occurs. A company must develop corporate values, enforce its own code of ethics and strive to prevent misconduct—even one as small as that of the case-client. The case of the ethical dilemma with this client would allow the team to extrapolate to a larger scenario and discuss what such a code would entail. The 2004 amendment to the FSGO requires that a business’s governing authority be informed about its ethics program with respect to content, implementation and effectiveness. This places the responsibility on the company’s leadership. In this case, leadership is lacking.

The accounting fraud of this client in this case is not totally dissimilar to the accounting scandals of the Twenty-First century such as WorldCom, Global Crossing, Qwest and Enron—and that of this case client—evidenced that falsifying financial reports had become part of the culture of many companies. The accounting/finance student’s response was particularly strong and shows that this student was aware of the recent history of similar situations. Such abuses increased demands to improve ethical standards in business and, thus, in 2002, Congress passed the Sarbanes-Oxley Act (SOX) which established broad change in organizational control and accounting regulations. SOX created an accounting oversight board that requires corporations to establish codes of ethics for financial reporting and to develop greater transparency in financial reports to investors and other interested parties. Although this company is small and
private and outside the reach of SOX, the team of students could make comparisons and point out that the law requires top executives to sign off on their firms’ financial reports and risk fines and prison sentences if they misrepresent their companies’ financial position. SOX and FSGO, therefore, have institutionalized the need to discover and address ethical and legal risk. The ethical dilemma and accounting fraud at issue in the case provide a perfect illustration for the students’ team to discuss the importance of the importance of developing formal and informal mechanisms to have transparency about issues associated with the risk of misconduct—be it in a small, private company or a large, public company.

The importance of developing an organizational ethical culture and a discussion of the benefits of business ethics should ensue. For example, discussion could take place about the future sale of the client’s business a year after the scenario and the fact that the sale of the business was most assuredly lower due to the accounting fraud. Also, the students could expand the discussion of stakeholder orientation to include the future buyer/investor in this business.

A survey of business ethics literature would allow the students to extrapolate questions to a larger firm: how did this ethical conduct contribute to employee commitment? To investor loyalty? To customer satisfaction? To increasing profits? To a profitable sale of the business?

The catalyst for the student’s response to the client’s admission of tax fraud was based on their individual moral philosophies and values. Although an investigation into these individual factors is a basis of ethical inquiry, in this case scenario, it would be more useful to briefly recognize the moral philosophies upon which an ethical inquiry is based, and then move the discussion to a framework of inquiry that includes a different analysis. A comparison of moral philosophies such as teleology, egoism, utilitarianism, deontology, virtue ethics and justice is usually part of a business ethics class and a review of the literature and studies is part of most business ethics text books. This team of students would benefit by expanding their ethical discussions from the moral and philosophical discussion to one that embraces stakeholder relationships, social responsibility and corporate governance.

If the owner takes money out of the cash register does this not transmit the owner’s values to his employees and establish a corporate culture of theft? If the owner/manager cheats how this does affect their customers and other owners or investors?