

IT'S A WONDERFUL LIFE: A CASE STUDY IN ACCOUNTING PROFESSIONAL ETHICS AND CONDUCT

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Abstract

The popular holiday movie, *It's a Wonderful Life*, provides a useful case study that illustrates various topics in accounting ethics and professional conduct. These topics are particularly of interest and use to new and future accountants. We discuss our use of the film and provide questions and notes corresponding to relevant sequences in the film that stimulate discussion and thought. Accounting students respond positively to the film in terms of its usefulness and appropriateness.

INTRODUCTION

In 1998, Arthur Levitt, Chairman of the Securities and Exchange Commission, delivered a biting speech on business and accounting issues at New York University's Center for Law and Business. Levitt expressed concern over corporate earnings management, adding that it may lead to "manipulation," and promising that the SEC would "...root out and aggressively act on abuses of the financial reporting process" (Rankin, 1999). Additionally, the financial "Perfect Storm" of Enron and Worldcom has led "Critics in the media, Congress and

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elsewhere...” to “...call into question...the integrity of ...” corporate management and the accounting profession (Thomas, 2002).

Although Levitt, Congress, and others have been recently calling for an emphasis on ethics and integrity, professional bodies (AICPA, ICMA, IIA, etc.), academicians and researchers have addressed the issues for several years. Fox (1981) and others include leadership, integrity and ethical training as priorities in business and accounting education. The curricular discussions on the role and affect of integrity and business ethics were a premonition of the financial spectacles observed in 2002. For two decades the business and accounting curriculums have responded, becoming broader and including ethics training. Yet, the crisis of today relates directly to the areas the curriculum was striving to strengthen. The balance of this paper will focus on the use of a popular film to provide an additional pedagogy in the delivery of accounting professional ethics education.

Several popular films include business-related ethical issues as key elements of their plots. *Wall Street* (1987), *Other People's Money* (1991), and *Barbarians at the Gate* (1993) present thought-provoking sequences based on the 1980's takeover activity. Dyl (1991) and Belden (1992) propose and test the use of *Wall Street* as a case that highlights mergers/acquisitions and ethics. Chan, Weber and Johnson (1995) identify key issues in takeovers and corporate financial management in *Other People's Money*. Similarly, Nofsinger (1995) and Peterson and Philpot (1997) develop cases in corporation financial management using the film *Barbarians at the Gate*, which is based on the actual takeover of RJR Nabisco.

We propose director Frank Capra's popular holiday classic, *It's a Wonderful Life* (*WL*), as a case that illustrates key concepts in accounting professional ethics and professional conduct. While other films have highlighted corporate financial management issues, *WL* is particularly useful to new and future accountants, given the timeliness of the issues addressed by the film. We provide a description of our use of *WL* as a classroom case suitable

for undergraduate students or newly-hired accountants, complete with a questionnaire corresponding to relevant sequences in the film.

OUR USE OF THE FILM

The protagonist of *WL*, George Bailey, manages a mutual savings bank in a small north-eastern city. He runs the mutual in the face of the Great Depression and the constant competition and harassment of Henry Potter, the owner of the local commercial bank. An angel spares George from a Christmas Eve suicide (after business has gone bad) and shows George what the town would have been like in his absence.

We use *WL* to provide life-like illustrations of dilemmas commonly faced by newly hired (as well as senior) professional accountants. As such, the film is appropriate for use in such undergraduate courses as auditing, theory, professional ethics or for use in continuing professional training in ethics. Sequences from the film provide vignettes that provoke student thought and discussion. The film addresses common topics including: conflict with superiors, corporate governance and mission, law versus ethics, perquisites, and whistle-blowing. Several sequences in *WL* also provide opportunity to discuss ethical and market/social issues (such as child labor law, competitive markets, and business social responsibility), and a separate case could be devoted to these topics. We limit our discussion in this case to issues dealing directly with accounting professional ethics and conduct.

WL is a lengthy film with a total running time of 129 minutes. Fortunately, as a holiday television staple, the film's plot and premise are quite familiar to most viewers. Also, the sequences related to accounting professional ethics have a combined running time of approximately 35 minutes, so using a DVD or videotape to fast-forward can effectively save time yet not impede plot continuity for the students. The accompanying exhibit contains times and titles of relevant sequences and questions and notes related to these sequences. We have used the *WL* case in an introductory undergraduate course. Casual observation of students

indicate that the students enjoy the film as a break from the normal lecture routine, and students find watching a popular film from a critical, rather than an entertainment, perspective to be challenging. Students also view the *WL* case as a constructive use of class time.

CONCLUSION

While several popular films have been used to illustrate important topics in corporate financial management, little (if any) has been done to develop illustrative popular film cases in accounting professional ethics. The classic film, *It's a Wonderful Life*, contains several well-filmed sequences that do so. Our use of the film provides a single-class-session case analysis that provokes student thought regarding financial institution history, regulation and management, segregation of duties, personal use of corporate assets, and ethical dilemmas in a format that is well-received by students.

Exhibit: Viewing Questions and Notes for *It's a Wonderful Life*

1. Sequence start time: 8:30 Sequence title: Drugstore

Q: Mr. Gower has sent George to deliver a poisonous prescription. How should an employee respond when a supervisor may not be in control of his/her faculties and the employee believes the supervisor to be negligent in the conduct of his/her duties?

Note: With the knowledge that Gower placed the poison in the medication, George, aware that a customer is in danger of loss of life, should disobey the directive and document his observations in writing. George should then deliver his written observations to Gower for review. Gower was distressed but we also know that he was a professional and would have appreciated the challenge. Many times it is not the challenge that generates bad feelings - it is the manner in which the challenge is presented.

In situations requiring ethical decision making Steven Mintz (1996) provides the following framework to evaluate the "...ethical propriety of decisions:" (p. 35)

1. Determine the facts.
2. Identify the operational issues.
3. Identify the accounting/business issues.
4. Identify the stakeholders and obligations.
5. Make an ethical analysis of the alternatives.
 - Is it legal?
 - Is it consistent with professional standards?
 - Is it consistent with in-house rules?
 - Is it right?
 - Is it fair?
 - Is it beneficial?
 - Is it consistent with virtue considerations?
6. Decide on a course of action.
7. Double-check your decision-question it.
 - How would I feel if my decision were printed in the local newspaper?
 - How would I feel if my family found out about my decision? (p.35-36)

Q: George is faced with a choice: obey the directive of Mr. Gower or disobey the directive of Mr. Gower. How should an employee approach such a dilemma?

Note: With the knowledge that Gower placed poison in the medication, the ethical decision making model would support the disobey choice. However, given George's age his decision to see his father was a good choice, especially considering the Gower's condition. Peter Bailey could then return with George to the drugstore and verify contents of the prescription with Gower. In a normal employee relationship within a larger company there would

be policies and procedures identified in the employee manual for resolving such conflicts.

2. Sequence start time: 8:44 Sequence title: Peter Bailey Meets with Potter

Q: Potter accuses Peter Bailey of running a charity. What is the appropriate role of charitable giving by publicly-owned corporations?

Note: It can be argued that there is no reason for a public corporation to make donations. Friedman (1970) likens managers' discretionary spending of corporate resources on charity to the taxation and spending function of government, the tax falling on stockholders (lower profits), employees (lower wages), and/or customers (higher prices). Because free societies require that taxation and spending decisions be made by popularly-elected officials, Friedman posits that effective corporate charity requires corporate officers be popularly elected, rather than hired by stockholders. The logical conclusion is a socialist society in which economic resources are directed by politics, rather than by the market.

Some charitable work by corporations may be justified as public relations marketing when employed to advantage the company's market position or when it constitutes legitimate employee perquisites consistent with prevailing labor market wage rates. However, Friedman states that the clearest corporate policy is to maximize corporate profits, which can be distributed to shareholders who can then support the charities of their choice.

Q: Peter Bailey defends his forbearance by stating that times are hard. Does a lender have a moral obligation to forebear based on macroeconomic conditions?

Note: Bailey's statement implies a moral obligation to work with borrowers when times are hard. From a practical perspective, if the economy is slow (The date depicted in this scene is approximately 1919, the trough of the postwar recession.), a lender may have more difficulty efficiently liquidating repossessed assets than getting a borrower to resume payments. As a mutual institution, Bailey Brothers is in the unique position of having borrowers who are also owners, thus a forbearance policy is never against the interests of *all* owners.

3. Sequence start time: 30.23 Sequence title: B&L Board of Directors Meeting

Q: What is the role of a member of the Board of Directors of a corporation? Does Potter represent his interests as a proponent of the B&L or his personal interest as a competitor? Is it ethical to operate a "linked" board? Can such a board adequately represent the interests of stockholders/independent investors?

Note: Directors serve as agents of the shareholders. The most important role of the Board is the selection and monitoring of the management team, which serves as agents of the board. Potter shows his colors by his motion to dissolve the building and loan, the dissolution of the building and loan would lead to improved profit performance of his other investment interests. Although linked boards are prohibited for publicly held companies, linked boards are common in small communities. To the extent that the board of directors is to represent the owners and the competitor owns a portion of the business there does not exist an ethical issue. However, should the competitor owner attempt to pursue activities that would lead to negative consequences for independent owners, the result would be violations of ethical standards, fiduciary duty and applicable law.

Q: Potter identifies Peter Bailey as a man of high ideals, implying that his commitment to high ideals prevented him from making good business decisions. Can a person make good business decisions without sacrificing ideals? Does violating ideals lead to more profitable business decisions?

Note: Hollywood often portrays the wealthy as greedy, calculating and ruthless committing crime after crime only to have highly-paid personal attorneys get them off through legal loopholes or by bribing legal and political figures. Contrary to this depiction, there is no evidence that managers or owners who have high ideals make poor business decisions or generate lower profits. In fact, companies which dearly hold to ethical business practices have outperformed their competitors. For example, Johnson and Johnson reaped market advantages through consumer favor in how they handled the Tylenol tainting.

Q: Potter controls the bus line, department store, bank, and rental properties. Does a business' diversifying into other business lines manipulate market forces and exploit consumers? Should a corporate board of directors diversify corporate investments away from core business interests?

Note: Exploitation may result if Potter “corners on the market” on key services or products. However, in a free market economy one firm's excessive profit will attract other firms, providing competition and ultimately lowering the price of goods and services to all consumers. As for corporate diversification, shareholders can diversify their personal portfolios with lower cost and less risk. The purchase of a specific stock is motivated by the corporation's core business activities.

4. Sequence start time: 50:00 Sequence title:
Marriage/bank run

Q: Sam Wainwright offers George Bailey a stock tip over the telephone. Is this illegal insider information? What is the ethical consideration?

Note: This sequence is set in 1928. The Securities and Exchange Act of 1934 prohibited trading based on “material, nonpublic information” and established penalties for insider trading. Thus, at the time, this was not illegal by statute. Widespread security market manipulation prompted passage of the act. This is a classic case of an action being perfectly legal, but ethically questionable. From an ethical perspective, George might consider that acting on the tip would involve purchasing shares from other investors at a price that was below true market value. George knows the true value only via private information, thus he would be exploiting an unearned information advantage. Interestingly, there is no evidence in the film that George acted on the tip, but there is evidence that doing so would have been profitable.

5. Sequence start time: 1:04:00 Sequence title: Bailey Park

Q: Potter offers George a salary of \$20,000 per year (9 times his Building and Loan salary) plus travel and executive “perks.” Is it unethical to research the personal desires and aspirations of competitors and pursue guerilla tactics to destroy or critically wound a competitor by hiring away “key” officers or employees?

Note: Many companies recognize the contribution of key personnel and may want to hurt a competitor by hiring one or more of their key employees. If a company has an opening for a specific job requiring unique skills possessed by a competitor’s key employee, there is nothing unethical about pursuing the qualified potential employee. However, the creation of an unnecessary position to lure a competitor’s key employee would be unethical.

6. Sequence start time: 1:16:50 Sequence title: Christmas Eve:

Q: George jokingly informs the bank examiner that “Between you and me, Mr. Carter, we are broke!” to which Carter replies “I shouldn’t wonder when you OK reverse charges on personal long distance calls.” Is it ethical to conduct personal business or personal visits and communication during business hours? Is it unethical to have the employer pay postage or long distance charges for personal communication? When are personal expenses acceptable, and when are they fraud?

Note: Conducting personal business while at work is always an unethical activity. Employees are engaged to provide services to an employer, and as such give up the right to use business hours for any type of personal activity. Many employees rationalize the use of company resources, citing low pay or unpaid time as justification. In effect, the employee using company resources for personal activities obtains a financial benefit beyond his/her wage. Some employers permit and even encourage employees to take advantage of phone and postage, calling the benefits received. To the extent that these perquisites exceed *de minimus* rules, benefits received should be reported as income subject to federal and state tax withholding. If the employer knowingly allows employees to utilize company assets, the benefit satisfies the definition of income in the tax code. Therefore, an employer could collude with employees to defraud the government of legitimate tax. According to Mintz' (1996) ethical decision guidelines (and generally consistent with most professional codes of conduct), if it is not legal it is unethical.

Q: As an accountant, what should you do if you expect someone of submitting personal expenses for reimbursement?

Note: If suspecting someone of violating reimbursement policies of the company, the accountant should report suspected violations to their supervisor for appropriate handling.

Q: Management quality is an element of a bank examination, or any other audit. When Carter sees evidence of Violet kissing George, should this prompt character questions in Carter's mind? Do/should perceptions of someone's personal character influence opinions of his/her professional character?

Note: Many people use different ethical/integrity frameworks to manage different components of their lives. It is entirely possible that a manager may recognize a different (higher or lower) standard of loyalty to shareholders than to a spouse. It is important that auditors and examiners maintain objectivity.

Q: Uncle Billy was carrying \$8,000 (almost 4 times George's annual salary) of B&L money in an open envelope and took pleasure in goading Potter about the accomplishment of Harry Bailey. Was Uncle Billy performing his duties with due diligence?

Note: Employees have a responsibility for completion of business tasks before personal activity, even in an errand. Employees are expected to use due care in the handling and preservation of business assets.

Q: Potter discovers the \$8,000 of lost cash. What is his legal/ethical obligation regarding the money?

Note: Under common law, Potter is a bailee for the true owner of the money. If Bedford Falls is located in New York, as is suggested in the film, statute requires Potter to report the find to authorities, or he would be guilty of a misdemeanor. If the money is later determined to be abandoned, then Potter can claim title. However, Potter knows that the money belongs to the building and

loan and is intended for deposit. In keeping the money, Potter's actions are no longer subject to ethical questions; he is a thief.

Q: Potter knows that Uncle Billy has provided him a way to do irreparable harm to the Building and Loan. Potter must "play along" to ensure that Uncle Billy does not remember placing the envelope full of money in the newspaper and giving it to him. This provides Potter the "out," if Billy remembers placing the money in the newspaper, then Potter can produce the newspaper and the money, feigning ignorance. What should Potter have done with the \$8,000?

Note: Potter should have immediately called George, communicated the lax procedures followed by Uncle Billy in handling the \$8,000, and had a cashier at the bank count the money and credit the B&L deposit.

Q: Potter's assistant observes Potter's actions and knows that he is involved in an activity that is illegal. What dilemma now faces the assistant? What are his alternatives? Use the ethical decision framework presented earlier to assess each alternative. What do you recommend?

Note: Let's assume for argument that the assistant would not choose to be involved in theft. The assistant's options are, to do nothing and go along with whatever Potter decides to do next, to confront Potter with the illegality of his activity or to resign from his position with Potter and communicate the illegal activity to the authorities. In the ethical analysis of the assistant's position we find that it fails the first question in the analysis questions... Is it legal? Theft of \$8,000 is not legal and is clearly unethical. The best recommendation would be to confront Potter with the illegal activity and if he fails to do the right thing, resign from the position.

Q: When Potter confirms that Uncle Billy cannot account for the cash and moves against George, seeking an arrest warrant, Potter's assistant knows Potter's ultimate decision. What ethical dilemma now faces the assistant? How would you respond?

Note: Potter is now going to file a false police report with a knowingly false accusation which is both illegal and unethical. This situation leads to the dilemma of whether the assistant blow the whistle on Potter. What about “whistle blowing?” Should the assistant immediately go public or after resigning, go to authorities? In deciding whether or not to go public with concerns, many authorities on business ethics present a series of considerations:

1. Will the business do serious and considerable harm to the public?
2. If harm will result, the employee should take their concerns to the supervisor.
3. If the immediate supervisor does nothing, then the employee should pursue all other internal options before going public.
4. The “whistle blower” must possess clear documentation /evidence of the claim.
5. The employee must have reason to believe that going public will remedy the condition.

In this case the assistant does not know Potter's final action. Potter could file charges and later uncover the money, rescuing George from ruin. The best choice for the assistant would be to either resign or wait to see how far Potter will go with the charade. If Potter saves George – no harm done, if Potter lets George go to jail the assistant would be an accessory to Potter's crime and should go quietly public – probably to the FBI (Potter may control local law enforcement).

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