6-1994

Report Earnings Accurately

Kenneth Yale Rosenzweig
University of Dayton, krosenzweig1@udayton.edu

Marilyn Fischer
University of Dayton, mfsicher1@udayton.edu

Follow this and additional works at: http://ecommons.udayton.edu/acc_fac_pub

Part of the Accounting Commons, Business Administration, Management, and Operations Commons, Business Law, Public Responsibility, and Ethics Commons, Corporate Finance Commons, and the Nonprofit Administration and Management Commons

http://ecommons.udayton.edu/acc_fac_pub/2
REPORT EARNINGS ACCURATELY

As authors of the March article, "Is Managing Earnings Ethically Acceptable?" we wish to thank Alfred M. King for his letter in the April issue questioning some of the contentions in our article. In a time when corruption seems to be rampant in many aspects of our national life, it is important for accountants to discuss openly what are their ethical responsibilities and what are the limits to those responsibilities. The credibility of accounting numbers is vital to our success as a profession and as individual accountants. There will be no demand for accounting service if accounting information is not trusted by users. Accountants have incorporated into their ethical codes the obligation to present information fairly and in an undistorted manner.

Mr. King must have misunderstood our definition of earnings management. As we stated, earnings management includes the actions of a manager that serve to change current reported earnings without generating a corresponding change in the long-run economic profitability of the unit. Managers who change earnings in this way are trying to influence positively the perceptions of their unit by users of the earnings numbers when there have not been any changes in the operation of that unit to warrant it. This is manipulative and unethical. How can anyone question this?

Mr. King seems especially concerned about whether earnings management can come about through operating decisions. For example, how can the selling of excess assets be bad? We do not question whether it is good or bad to sell off excess assets; we question the timing of that decision by management during periods when earnings need to be enhanced or reduced. When the timing of the operating transaction is selected to influence earnings rather than for valid operational reasons, the earnings are distorted and users' interests may be damaged.

We have expressed in our article our qualms with limiting operating managers' range of action in making operating decisions and do not advocate a complex set of rules to prevent earnings management by operating decisions. We feel that a major part of the problems the accounting profession faces in the area of accounting manipulation is the excessive rules orientation toward the measurement of earnings. This perpetuates the view among accountants that if a transaction is permitted by the rules, it is justified. However, virtually all accountants recognize the significant ability to influence earnings by choice among alternative acceptable accounting rules.

Rather, we advocate that both accountants and managers commit themselves to the positive obligation to report earnings in an accurate and undistorted manner. No set of rules will ever be able to fully prevent earnings management due to the complexity and changing nature of business transactions and operations. In order to assure the provision of accurate and usable accounting information, it will be necessary to rely on the internalized ethical values of accountants and managers.

Kenneth Rosenzweig and Marilyn Fischer
University of Dayton

MANAGEMENT ACCOUNTING/June 1994