

# MANAGEMENT ACCOUNTANTS

Management accountants are the nuts and bolts of the decision-making process of companies. They provide forecasts on future business and economic events for long-term strategic planning, such as capital budgeting and project financing. They also provide management with necessary information for making short-term decisions such as optimum product mix, pricing of product, and leasing or buying activities. Given their unique roles and duties, management accountants may face a number of ethical challenges when discharging their duties.



## ETHICAL SCENARIOS



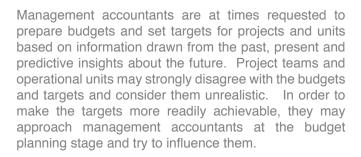
### **Pressure from the management** and colleagues

Is it true that "The boss is always right"? Should I follow the management's instruction even if it appears to be biased?



In order to project splendid financial performance and healthy financial position, senior management may exert pressure on management accountants to use aggressive or even unrealistic assumptions when making forecasts. Sometimes, management accountants may be asked to render analyses to support the personal ambition of some senior management staff.

Different project teams have approached me over their budget plans. Which one should I entertain?





**Insider dealing** 

I recommend my relatives and close friends to buy shares of my company. Is it fine?



Management accountants of listed companies may have access to the company's confidential information (e.g. merger and acquisition plans) which is likely to influence the share price of the company. They may face the temptation to disclose such highly sensitive information to friends and relatives prior to the public announcement.



Management accountants should be aware of the threats as well as understand the legal requirements under the Prevention of Bribery Ordinance (POBO) (Cap. 201) and other relevant legislations. The above situations create various threats to the fundamental principles of ethics for professional accountants.



#### PREVENTION OF BRIBERY ORDINANCE

According to Section 9 of the Prevention of Bribery Ordinance (POBO), an agent (e.g. an employee, a director), without the permission of his/her principal (e.g. the employer, the company) or any reasonable excuse, solicits or accepts any advantage for doing or forbearing to do any act in relation to his/her principal's affairs or business, shall be guilty of an offence.

Advantage refers to anything that is of value such as money, gift, commission, loan, employment, service or favour, except entertainment. Entertainment refers to the provision of food or drink for consumption on the occasion when it is provided, and any other entertainment connected with such provisions.

## CODE OF ETHICS FOR PROFESSIONAL ACCOUNTANTS

Fundamental principles of ethics for professional accountants

According to the Code of Ethics for Professional Accountants (COE) issued by the HKICPA, there are five fundamental principles of ethics for professional accountants (the fundamental principles):

- (a) Integrity to be straightforward and honest in all professional and business relationships.
- (b) **Objectivity** to exercise professional or business judgment without being compromised by:
  - (i) Bias:
  - (ii) Conflict of interest; or
  - (iii)Undue influence of, or undue reliance on, individuals, organizations, technology or other factors
- (c) **Professional Competence and due care** to:
  - (i) Attain and maintain professional knowledge and skill at the level required to ensure that a client or employing organization receives competent professional service, based on current technical and professional standards and relevant legislation; and
  - (ii) Act diligently and in accordance with applicable technical and professional standards.
- (d) **Confidentiality** to respect the confidentiality of information acquired as a result of professional and business relationships.
- (e) **Professional Behaviour** to:
  - (i) Comply with relevant laws and regulations;
  - (ii) Behave in a manner consistent with the profession's responsibility to act in the public interest in all professional activities and business relationships; and
  - (iii) Avoid any conduct that the professional accountant knows or should know might discredit the profession.

## CODE OF ETHICS FOR PROFESSIONAL ACCOUNTANTS (CONTINUED)

Unlawful Acts or Defaults by or on Behalf of a Member's Employer It is not practicable to set out all the offences which members may encounter in the course of their work but the principal statutory and common law offences concerned are:

- (a) theft, obtaining by deception, false accounting, and suppression of documents;
- (b) fraud, forgery and offences in relation to companies;
- (c) corruption offences;
- (d) bankruptcy or insolvency offences, frauds on creditors or customers, false trade descriptions, and offences arising out of relations between employers and employees;
- (e) conspiracy, soliciting or inciting to commit crime and attempting to commit crime;
- (f) offences in relation to taxation; and
- (g) insider dealing.

(Paragraph 500.1, section 500, Chapter C of the COE)

If a member acquires knowledge indicating that his employer or someone acting on behalf of his employer may have been guilty of some default or unlawful act, he should normally raise the matter with management internally at an appropriate level. If his concerns are not satisfactorily resolved, he should report the matter to non-executive directors and those charged with governance where these exist. Where this is not possible or fails to resolve the matter, a member may wish to consider making a report to a third party. Members in business should refer to section 260 under Chapter A of the COE, which sets out the response framework when members encounter non-compliance with laws and regulations during the course of their work. Local guidance is provided in section 500 of Chapter C of the COE on reporting suspected defaults or unlawful acts to third parties outside the organisation for which the member works.



# Pressure from the management and colleagues

Management accountants are responsible for analysing information to advise business strategy and drive sustainable business success. Such information may relate to macroeconomic indicators (e.g. inflation, interest rates and exchange rates), government policies and socio-political factors. As management accounting sometimes may involve subjective judgment made according to management's instructions, it may be subject to the undue influence of individual staff member, or be harnessed for personal advantage because of interpersonal rivalry in the organisation.

As professionals, management accountants are trusted to be ethical, accountable and mindful of the organisation's values, governance requirements and social responsibilities. They should be vigilant to all actual or potential conflicts of interest and not to put personal advantage or short-term considerations before the longer-term interests of the organisation and its stakeholders. In addition, they should always behave and be seen to behave with integrity and objectivity.

When preparing the budgets, they should ensure that the budgeting processes are transparent and consultative so that the parties concerned could have a better understanding of the budgets and in turn set targets in line with the key strategic priorities of the organisation. Moreover, they should engage individual project teams and operational units with the planning of activities and the setting of targets at an early stage to engender accountability.

Management accountants should always take heed of the requirements of the POBO, as well as the COE. Upon facing pressure from the management or colleagues, they should:

- decline any advantage which is offered with an intention to influence the bases of assumptions and forecasts:
- stand firm on their professional judgment or ethical practice in any circumstances; and
- use their professional knowledge and experience to constructively challenge any queries or decisions which may undermine the organisation's values.

Management accountants often encounter different risks while navigating their organisations forward, placing them in ethical dilemmas. A practical tool, a "GPS Ethics Compass", is introduced in the "Topic of Interest" section below to help accountants arrive at a sound decision when encountering ethical dilemmas.

#### KEY ISSUES AND TAKEAWAYS (CONTINUED)

### Insider dealing

As defined under the Securities and Futures Ordinance (SFO) (Cap. 571), insider dealing is a kind of market misconduct. In gist, insider dealing takes place when a person connected with a listed company possesses privileged information which could affect the share price when disclosed, and trades or persuades other persons to trade in the securities or derivatives of the company in order to make profits or avoid losses before the information becomes public knowledge. Therefore, accountants will breach the SFO even they do not trade themselves, but persuade their relatives or close friends to trade the securities prior to an announcement.

Handling insider information readily creates self-interest threat to the fundamental principle of confidentiality. Accountants should always respect confidentiality of the information acquired during their daily work. They should not disclose any such information to third parties without proper authority nor use the information for personal advantage of themselves or third parties.



### **CASE STUDY**

#### FINANCIAL CONTROLLER IS NO EASY JOB



Rex was employed as the Financial Controller of an expanding IT company which was planning to go public. In order to project a good financial performance, Andy, the Managing Director hinted that Rex should handle the financial estimates and anticipate sales growth meticulously.

Andy also made it clear to Rex that he did not care about what accounting method he would use.



In selecting the merchant bank to arrange for the listing, Rex's recommendation would be considered seriously by the board. Different bank managers approached Rex to promote their services.



Ben, who was the Marketing Director of ABC Bank, called Rex's office. After introducing the bank's offer, Ben further mentioned that he was currently handling acquisition plans of other listed companies.

He promised to release some "valuable information" to Rex if he helped him get the business. Rex did not take Ben's words seriously.



Based on the objective report Rex prepared, ABC Bank was engaged by the board to proceed with the listing of the company.

Finally, the company was successfully listed.

### CASE STUDY (CONTINUED)

#### FINANCIAL CONTROLLER IS NO EASY JOB





Rex divulged to Yuki, his wife that his company was undertaking some merger and acquisition plans which might boost the share price of the company. However, the Managing Director asked him to manipulate some management accounting data so as to facilitate the granting of credit facilities by some banks.

In a reunion of schoolmates, Yuki met Ben, one of her old best friends. Yuki sought advice from Ben regarding the difficulties her husband faced. Yuki did not know the relationship between Ben and her husband's company.



Ben called and invited Rex for dinner, saying that he would keep his promise of passing some "valuable information" to Rex.

Besides, he said he could offer golf club membership to Rex if he could provide some useful information about his company's merger and acquisition plans to him.



IF YOU WERE REX,
WHAT WOULD YOU DO?
HAS REX DONE ANYTHING WRONG?

#### **COMMENTARIES ON THE CASE**



#### **Financial Projection for Listing**

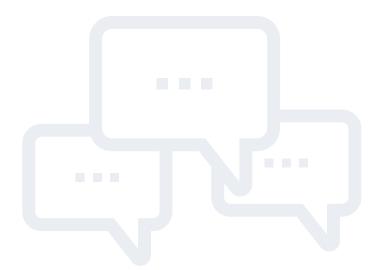
Rex should always handle the financial estimates and anticipate sales growth meticulously. He should **document his bases of assumptions** and agree them with the Managing Director. All these should be reviewed by the reporting accountant as well as the bank which sponsored the listing, and the eventual delivery of the forecasts would be a matter of public and regulatory scrutiny once the company got listed.

Although the Managing Director was not concerned with what accounting method Rex used, Rex should ensure that the accounting method complied with the **accounting standards** prescribed by law and regulation and was relevant to the company's circumstance.



#### **Request for Manipulation of Accounting Data**

Rex should explain to the Managing Director that, first of all, a wilful act of manipulation of accounting data would be a **criminal offence**. Secondly, accounting information presented to banks would most likely be audited. Once the banks realised that there were significant discrepancies between the management accounting data previously presented and the audited accounting data, they would ask for explanations which would well call into question the credibility of the company. In the worst case scenario, banks could withdraw the financial support to the company.





The "valuable information" provided by Ben was likely **insider information** which, if used to deal in listed securities, could cause severe legal consequences. Rex should make it clear to Ben that his evaluation of the bank was conducted in an objective manner and there would be no need for Ben to reciprocate with any "gift" for him.

Although having dinner with Ben was a social activity, Rex should still be careful. If Ben disclosed any valuable information during their conversation, Rex should not deal, counsel nor persuade other persons to deal in the securities. Otherwise, he would breach the **SFO**.

Rex would have committed an offence under the **POBO** if he accepted the golf club membership from Ben and disclosed to him the useful information about his company's merger and acquisition plans as a trade. In fact, Rex should clearly **reject** the offer and **report** to the Independent Commission Against Corruption (ICAC) if being offered a bribe.



#### **Handling of Confidential Information**

One of the fundamental principles which professional accountants should comply with is confidentiality. They should respect the confidentiality of information acquired as a result of professional and business relationships and, therefore, not disclose any such information to third parties without proper and specific authority, unless there is a legal or professional right or duty to disclose, nor use the information for the personal advantage of themselves or any third parties. Rex should be cautious not to disclose his company's merger and acquisition plans to anyone, including his wife and/or other relatives/friends, as such information was highly confidential and could affect the share price of the company.

## TOPIC OF INTEREST

#### A PRACTICAL TOOL FOR DECISION MAKING "GPS ETHICS COMPASS"

Integrity is a must-have quality for management accountants. Management of companies rely on the information provided and analyses made by management accountants to make strategic decisions. Management accountants should be conscientious in providing precise numbers without doctoring any information for ulterior motives. In addition, they should stay vigilant against corruption, fraud, malpractice and other unethical acts, and demonstrate moral courage to speak up and report any illegal acts or irregularities unveiled.

To help accountants arrive at a sound decision when encountering ethical dilemmas, the Hong Kong Business Ethics Development Centre (HKBEDC) has developed a practical tool, the "GPS" Ethics Compass. The Compass is like the Global Positioning System which shows them the right direction when navigating through different ethical challenges.

Guide your decision making with each of the four pointers of the following ethics compass before choosing the most appropriate course of action.

#### Legal requirements

Examples include the POBO, the SFO and the Companies Ordinance.

#### **Professional & self-values**

Integrity, objectivity, professional competence and due care, etc. as defined in the COE issued by the HKICPA.



Rules & guidelines

Examples include the Listing Rules for listed companies, guidelines set by the organisation.

#### Stakeholders' interests

Examples include the board, shareholders, investing public, employees, suppliers and customers.

## TOPIC OF INTEREST (CONTINUED)

Perform the roles of a management accountant properly:

- · acquire, develop and analyse financial information honestly so that management has reliable figures on which to base their critical strategic decisions. Unethical management accounting could result in misleading numbers which may result in production stoppage, stock out, delivery delay, wastage, financial decline, reputation damage, etc.
  - endeavour to put brakes on poor management strategies or decisions.
- · report to the management and the relevant authority any unethical concerns, conflicts of interest, malpractices or illegal acts unveiled.

Sunshine test should always be applied to assess whether the issue under concern can be discussed openly and the decision disclosed without misgivings.

After going through the above steps, select an appropriate course of action which can maximise the important values and interests of all stakeholders. Make a commitment to the choice and implement it. Please refer to the "Toolkit on Directors' Ethics" (link as below) for more information and application of the "GPS" Ethics Compass:

https://hkbedc.icac.hk/en/short/?code=director-ethics



Established under the auspices of the Community Relations Department of the ICAC, Hong Kong Business Ethics Development Centre (HKBEDC) aims to promote business and professional ethics on a long-term basis to sustain a level-playing field in Hong Kong. We offer free ethics training and consultancy services for business organisations and professional bodies.





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