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Boiling the Frog Slowly: The Immersion of C-Suite Financial Executives into Fraud

Original Paper Published: 27 July 2018

Volume 162, pages 645–673 (2020) Cite this article



Journal of Business Ethics

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> "Once you start on that slippery slope of evil, there is no going back for the vast majority of people." Phillip Zimbardo (Mechanic 2015).

Abstract

This study explores *how* financial executives retrospectively account for their crossing the line into financial statement fraud while acting within or reacting to a financialized corporate environment. We conduct our investigation through face-to-face interviews with 13 former C-suite financial executives who were involved in and indicted for major cases of accounting fraud. Five different themes of *accounts* emerged from the narratives, characterizing executives' fraud immersion as a meaning-making process by which the particulars of the proximal social context (the influence of social actors and contextual characteristics) and individual motivations collectively molded executives' vocabularies of fraud immersion. Our executives' narratives portray their fraud entanglement as typically occurring in small, incremental steps. Their accounts expand our understanding of the influence of socialization on executive-level financial fraud beyond the individualized focus of the fraud triangle model.

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Notes

1. Investopedia defines C-suite as “A widely-used slang term used to collectively refer to a corporation’s most important senior executives.” http://www.investopedia.com/terms/c/c-suite.asp#ixzz3rTzagDci.

2. According to the Free Dictionary Definition, a person crosses the line when his/her behavior changes from being acceptable to being unacceptable (accessed at http://idioms.thefreedictionary.com/cross+the+line).

3. The average annual revenue was computed based on each company’s last three years net sales before the fraud was discovered. The revenue (or net sales) information was obtained from http://www.sec.gov/Archives/edgar/data and articles published by Forbes, USA Today, or News Center.

4. Financialization is defined as the powerful role of financial markets and financial actors in shaping the behavior of firms and individuals, advancing the rhetoric of shareholder value maximization (e.g., Cushen 2013; Davis and Kim 2015; Ezzamel et al. 2008; Newberry and Robb 2008; van der Zwan 2014).

5. Of the 13 participants, all faced federal criminal charges for accounting fraud. Five entered into plea bargains as cooperating witnesses, avoiding jail time. The remaining eight participants were convicted in court trials and sentenced to jail.

6. With respect to social context, the importance of organizational factors such as tone at the top and organizational climate has been documented in prior research and practitioner frameworks in accounting (Murphy and Free 2016).

7. To date, “there appears to be at least eight types of rationalizations:” denial of responsibility, denial of injury, social weighting, denial of victim, appeal to higher loyalties, legality, metaphor of the ledger, and refocusing attention

(Ashforth and Anand 2003, p. 17). The first five rationalizations are identified by Sykes and Matza (1957) and the remaining are identified by Gellerman (1986), Klockars (1974) and Ashforth and Kreiner (1999), respectively.

8. We obtained contact information from a private investigator (51), a former FBI agent from the fraud division (16), a journalist (1), fraud conference speakers (2), and LinkedIn (34).

9. In contrast, Free and Murphy (2015) focus more broadly on 'why' prison inmates (executives and non-executives) co-offended or cooperated with a group of two or more to engage in white-collar crimes, which ranged from financial reporting fraud to false information in mortgage applications to false real estate appraisals to improper disclosure of stock-market transaction fees to the use of falsified reports to a government regulator to mortgage fraud and wire fraud to asset misappropriation to corruption. Only 5 of 37 interviewees (white-collar criminals) were executives involved in financial reporting fraud.

10. Under a confidentiality agreement intended to protect our participants' identity, we do not disclose the industries of their employers.

11. While it is possible that psychopaths with extroverted personal charisma and charm are more willing to share their stories than non-psychopaths (e.g., Babiak et al. 2010; Boddy 2011; Hare 1993), we do not believe our results are contaminated because of the difficulty, along with a considerable amount of time and effort, we experienced in convincing the 13 fraud perpetrators to participate in our study.

12. During the first interview, the participant was sensitive to the word "fraud," showing a state of extreme discomfort and unwillingness to utter the word. Based on this reaction, we modified the questionnaire by replacing the word 'fraud' with 'crossing the line.' Observing how sensitive participants were during the interviews, we took extra care to not antagonize them and make

them feel comfortable about sharing their experience in accounting fraud. The revised interview questionnaire was used for the subsequent twelve interviews. The narratives of the first interview were included in the main study as concern about potential data contamination is minimal in qualitative research compared to quantitative research (e.g., Holloway 1997, p. 121).

13. It took us a considerable amount of effort and time to convince the participants to voluntarily join our study. In 2011, we did not have all 13 interviews scheduled for the study. As we started with one interview, we were also contacting other executives. This effort lasted for 5 years before all interviews were completed.

14. The interviewers followed the approach used by Gendron and Spira (2010), seeking "to be perceived as empathetically neutral, caring about the [financial executives' meaning on becoming involved in fraud], while endeavoring to take a neutral stance toward emerging content…" (p. 280).

15. According to Smith (2008, p. 40), "…IPA aims to explore in detail participants' personal lived experience and how participants make sense of that personal experience. It is phenomenological in its concern with individuals' perceptions of objects or events, but IPA also recognizes the central role for the analysis in making sense of that personal experience and issues, strongly connected to the interpretative tradition. The participant is trying to make sense of their personal and social world; the researcher is trying to make sense of the participant trying to make sense of their personal and social world."

16. Financialized corporate environment refers to "the increasingly significant role of financial markets, financial actors and financial motives in daily life [of a company]" (Cushen 2013, p. 314).

17. Our interviewees' sensitivity to key financial metrics such as stock prices and

EPS resonates with the CFO survey responses reported by Dichev et al. (2013). The authors find that the desire to influence stock prices and Wall Street pressure to hit earnings targets are some of the main reasons as to why companies manage earnings.

18. From the interview narratives, we found that Jose's aspiration for success dated back to his earlier years when he visualized his notion of success, as opposed to failure, by thinking of an image of a white collar person in a business environment respected for his mind versus a blue collar worker with a lunch pail and tool belt.

19. Compliance means acquiescence to a request, whereas social conformity refers to the act of changing one's behavior to match the responses of other social actors (Cialdini et al. 1999; Cialdini and Goldstein 2005; Moore and Gino 2013).

20. The specific descriptions of each position are tied to the executive's reporting responsibilities. It was Jack's duty as a CAO to keep the programs in compliance and move money out of the intercompany account. Fred explained that he had to capitalize expenses to get the company through the first IPO and please Wall Street. Tom said that he had to find reserves to help the CFO manage earnings. James claimed that he had to find legitimate options for his company to meet the EPS forecast. Bobby was told to keep the write-offs under the lowest threshold. Ralph and James had to release financial reports on timely manner or before the competitors.

21. Cam's court records show a disgorgement order of $10–15 million dollars and a restitution order of $2–4 million dollars.

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Acknowledgements

The authors appreciate the insightful comments of David Cooper, Abe de Jong, James Holstein, Donald Palmer, Robin Roberts, Robert W. Scapens, Paula M.G. van Veen-Dirks, the participants in the 2014 American Accounting Association (AAA) annual meeting and the 2014 Accounting, Behavior, and Organizations (ABO) meeting, and the seminar participants at University of Groningen, in particular Henk ter Bogt. The authors have received research grants from the Center for Audit Quality (CAQ) ($15,000 US dollars) and PwC INQuires ($10,000 US dollars). In addition, this study has received research funding from the College of Business of Marquette University (Ikseon Suh) ($2500 US dollars) and the University of Groningen (Kristina Linke) ($3530 US dollars). Without this financial support, the completion of the study would not have been possible. The views expressed in this study are those of the authors and do not necessarily represent the views of the

CAQ and PwC. This paper was the 2015–2016 recipient of the Glen McLaughlin Prize ($10,000 US dollars) for Research in Accounting Ethics from the Steed School of Accounting (University of Oklahoma). The authors are grateful for the research grant/funding received and the research award.

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Ethics declarations

Conflict of interest

The authors declare no conflict of interest with the institutions that have provided research grants/funding or awarded this study.

Ethical Approval

All procedures performed in studies involving human participants were in accordance with the ethical standards of the institutional and/or national research

committee and with the 1964 Helsinki declaration and its later amendments or comparable ethical standards.

Informed Consent

Informed consent was obtained from all individual participants included in the study.

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Cite this article

Suh, I., Sweeney, J.T., Linke, K. *et al.* Boiling the Frog Slowly: The Immersion of C-Suite Financial Executives into Fraud. *J Bus Ethics* **162**, 645–673 (2020). https://doi.org/10.1007/s10551-018-3982-3

Received	Accepted	Published
16 January 2018	19 July 2018	27 July 2018
Version of record	Issue date	
27 July 2018	March 2020	

DOI
https://doi.org/10.1007/s10551-018-3982-3

Keywords

Financial statement fraud | Incrementalism | Slippery slope | Socialization

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