

Case Study #1: Expense Reclassification and Financial Statement Integrity

Background

You are the new CFO of a Canadian energy company that operates in a competitive and capital-intensive industry. Your board is pressuring you to improve key financial metrics, including cost-per-barrel figures and overall profit margins.

During a quarterly review, your team discovers that approximately C\$300 million in regular operating expenses were reclassified as capital expenditures over the past two years.

This reclassification significantly boosted the company's financial performance on paper but appears inconsistent with accounting standards. The journal entries involved are vague, often rounded, and lack supporting documentation. The company's external auditors have now flagged the issue, and a restatement of financial results seems likely.

You are facing a major ethical dilemma. The restatement will likely cause reputational damage, reduce investor confidence, and may result in legal action. At the same time, failing to address the issue could lead to regulatory penalties and personal liability.

The Situation Escalates

Despite your concerns, pressure continues from senior leadership and the board to maintain performance targets. The reclassified expenses are still being used in investor presentations, and the audit committee seems reluctant to probe further.

External auditors begin asking for backup documentation. When inconsistencies are exposed, the company is forced to restate its financial results going back multiple years.

Media coverage is swift, linking the issue to inflated executive bonuses and broken investor trust. Regulatory investigations are launched in both Canada and the U.S.

As CFO, you are now navigating shareholder lawsuits, reputational fallout, and tense board discussions. Some executives push back, insisting "everyone does this." Your leadership and ethical credibility are on the line.

Group Discussion Questions

1. What are the potential ethical issues in this situation?
2. How can you handle the stakeholders?
3. What steps can you take to protect your role and uphold your duties?
4. How can you prevent this in the future?
5. Have you ever encountered such a situation?