

The Effect of Rankings on Honesty in Budget Reporting

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Abstract:

We conduct an experiment to investigate the effect of rankings, which are pervasive in practice, on the honesty of managers' budget reports, which is important for sound decision making in organizations. Participants in our experiment are ranked in one of four ways: (1) firm profit, (2) own compensation, (3) both firm profit and own compensation, and (4) randomly, which serves as our baseline condition. None of the rankings affect participants' remuneration. Compared to our baseline (random rankings) setting, where participants indeed exhibit honesty concerns, we find that rankings based on firm profit significantly increase honesty and that rankings based on own compensation significantly decrease honesty. Participants who received both rankings were significantly more honest than participants in the own compensation rankings condition. We did not, however, find significant differences in honesty between the both rankings and firm profit rankings conditions. As such, participants in the both rankings condition seemed to focus more on the firm profit metric than on the financially congruent own compensation metric. We also find that our results are stable across periods, suggesting that the effects of rankings neither increased nor dissipated over time. We discuss the contributions of our study and concomitant findings to accounting research and practice.