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## A. A. FITZGERALD ON THE “PRINCIPLES OF ACCOUNTING”

Foreword by Louis Goldberg

### EDITOR'S INTRODUCTION

In recognition of the Fiftieth Anniversary of the publication of *A Statement of Accounting Principles* by Thomas Henry Sanders, Henry Rand Hatfield, and Underhill Moore, we are pleased to reprint the point of view of A. A. Fitzgerald and to provide a specially prepared Foreword on Fitzgerald himself, written by Professor Louis Goldberg. In an age when the controversy and comparison of normative and positive views of accounting theory continues — it is our view that a reconsideration of this material is appropriate. Copies of *A Statement of Accounting Principles* are available at a nominal price from the American Accounting Association offices.

Further commentary on Fitzgerald, the study itself and related matters can be found in several writings including:

R. J. Chambers, L. Goldberg and R. L. Mathews [Eds.], *The Accounting Frontier: In Honour of Sir Alexander Fitzgerald* [F. W. Cheshire, Melbourne: 1965].

M. Chatfield, *A History of Accounting Thought*, pp. 239 ff, 288, and 296. [Dryden Press, Hinsdale, Ill: 1974].

H. T. Deinzer, *Development of Accounting Thought*, pp. 17 ff, 147. [Holt, Rinehart, Winston, New York: 1965].

G. J. Previts and B. D. Merino, *A History of Accounting in America*, pp. 261-290 passim. [Ronald Press/John Wiley & Sons, 1979].

S. A. Zeff, *Forging Accounting Principles in Five Countries: A History and An Analysis of Trends*, p. 131 ff. [Stipes Publishing Co., Champaign, Ill: 1972].

\_\_\_\_\_. *Forging Accounting Principles in Australia*, p. 29 ff. [Australian Society of Accountants, Melbourne: 1973].

## FOREWORD

In Australia, Adolf Alexander Fitzgerald (1890-1969) was the outstanding accounting figure of his time. Practitioner, academic, lecturer, writer and editor, researcher, advisor to governments and active participant in many economic, financial and accounting issues, office-bearer in professional and cultural organizations, member and, in several cases, chairman of governmental bodies, director of companies; all these were part of his life and its achievements. For services to the Australian community he received acclaimed recognition by the award of Officer of the British Empire (O.B.E.) in 1953, and Knight Bachelor (Kt) in 1955, when he became entitled to be known as Sir Alexander Fitzgerald.

When he was appointed to the chair of accounting at the University of Melbourne in 1954, he became the first professor of accounting in any Australian university; he held this appointment until 1958.

At the time he wrote this article he was editor of *The Australian Accountant* and I believe he thought one of his functions as editor was to bring the latest and the best in overseas developments and opinions into the range of at least the potential cognizance of accountants in Australia. In carrying out this function, he regarded himself (in my opinion) as an analytical reporter of happenings in other countries.

In bringing the Sanders, Hatfield and Moore study to the attention of Australian accountants, Fitzgerald hails it as an important contribution, which, indeed, it clearly was. He draws a distinction between a principle, which he defines as "a fundamental truth used as a basis of reasoning" and a convention, which is "merely a generally accepted practice, which may or may not be based upon reasoned analysis". However, he does not examine the nature of a "fundamental truth" and so does not consider the relativity of "truth" or the degree of acceptance implicit in the "fundamentalism" of it. Hence, he does not ask what difference, if any, there may be between one generally accepted practice which, while based upon reasoned analysis, could still fall within his definition of a convention, and another which is developed by reasoning from the basis of a fundamental truth; if the reasoning process is the same the difference can only lie in the axioms or accepted propositions from which it starts.

He points out that the adoption of principles would remove many uncertainties, and he furnishes examples, one of which — the use of the term "reserve fund" — he had discussed at length

two years previously in a paper on Accounting Terminology [Fitzgerald, 1936, pp. 142-149]. He suggests that, except for a few differences in terminology and classification, arising mainly from differing legal requirements, the Sanders, Hatfield and Moore Statement was applicable to Australia. He points out, however, that in its concentration on the published reports of corporations the Statement seemed to ignore the problems faced by "internal" accountants.

It will be recalled that the Statement was one of the very early contributions in the long-running search for accounting principles which stemmed from the U.S. legislation in 1933 and 1934 relating to corporation securities. While the label "principles" may have been forsaken in the course of discussion over the next half-century, the substance of what was being sought has not changed fundamentally; accountants are still looking for a security blanket of theory to protect them from misinterpretation of accounting "circumstances" or "situations." A number of standards are currently in force which govern much of the accounting treatment of numerous controversial items, but the relation of many of these specifications to underlying "principles" or "conceptual framework" or theory is often unclear.

In the half-century since the article appeared, not only has much discussion taken place, among academics and professional accountants alike, but much practice has changed, as well as much of the economic and financial environment. Technological developments have greatly affected the process of amassing and colligating data, and the approach to auditing is now based much more on analytical perceptiveness and emphasis on internal control than the earlier tick-and-tot verificatory methods. In 1938 the holding company, while not unknown in Australia, was still a minority form of structure in corporate organization [Goldberg and Hocking, 1949], whereas nowadays it would be rare indeed to find a publicly listed company which does not have subsidiaries and hence require consolidated financial statements.

A series of statutory amendments to company legislation, which in 1938 differed from state to state, have greatly increased the obligations for disclosure of information in company annual reports and these obligations have applied nationally since the adoption of "uniform" company legislation in 1961. Since that year the several states have had the same statutory requirements for all incorporated companies, differing only in minor aspects to conform to strictly local cir-

cumstances, so that now all companies, irrespective of the state or territory of registration, are subject to the same set of statutory provisions and regulations. A National Companies and Securities Commission (NCSC) has been set up under Commonwealth legislation to monitor and oversee company activities; it operates both directly and through state Corporate Affairs Commissioners, who have taken over most of the tasks previously carried out by the State Registrars of Companies; these tasks include checking of prospectuses, registration and incorporation of companies, reception and custody of annual returns comprising both financial and non-financial information, removal of defunct companies from the register, and the like. The stock exchanges also have tended to act in unison in requiring listed companies to provide more timely information.

Company reporting has also been affected by the joint publication of standards by and in the name of the two predominant professional accountancy bodies, The Institute of Chartered Accountants in Australia (ICAA) and The Australian Society of Accountants (ASA). These standards are prepared by the Australian Accountancy Research Foundation (AARF), a body which was set up jointly by the two professional bodies in 1965. In the last few years the standards have been subject to review and approval of an Accounting Standards Review Board (ASRB), appointed by a Federal Minister to monitor them; such approval now gives a standard the force of law.

The task of developing and maintaining "Statements of Accounting Concepts and Statements of Accounting Standards" has been vested in two boards within the AARF — an Accounting Standards Board and a Public Sector Accounting Standards Board. The professional bodies nominate the members of these boards, which are supported by the full-time technical staff of the Foundation. Approval for public issue of any Standard lies with the National Councils of the ICAA and ASA.

The development of a Standard involves an extensive "due process" which is "considered essential to ensure that all interested parties are given ample opportunity to express their views and to ensure that the concepts and standards so developed are relevant, consistent and logically derived." This process comprises (1) initiation of a project by a Board "in response to the identification of emerging issues", (2) appointment of a Project Advisory Panel to review progress and serve as a resource base for a project, (3) preparation of a discussion paper or an "accounting theory monograph" by an external contractor or a Foundation staff member, (4) preparation by

the contractor and discussion by the Board(s) of a "key decisions questionnaire" identifying the principal issues to be resolved in a proposed Standard or Statement of Concepts, (5)-preparation of a "draft exposure draft", (6) refinement of the draft exposure draft by the Board(s) and distribution for comment to selected people regarded as knowledgeable of, interested in or involved with the topic, (7) review and amendment of the draft exposure draft in the light of responses received, (8) distribution of an exposure draft inviting comments from interested parties, with a simultaneous press release, advertisement in business newspapers and an insert or article in the monthly journals of the two bodies drawing attention to the exposure draft (the Foundation has a registrant mailing list of some 10,000 names, while the professional journals are sent to over 86,000 people), (9) preparation of a draft Standard or Statement of Accounting Concepts after full consideration of views expressed in the former stages, (10) if deemed necessary or advisable, a further selective exposure of a "refined" draft, (11) submission to the National Councils of the professional bodies for approval, (12) if approved, issue of the Standard or Statement by the National Councils.

In the light of such developments as these, Fitzgerald would no doubt freely, and perhaps gladly, acknowledge that the quantum of information in the annual reports of companies — at least of those listed on the stock exchanges, which are of most concern to the general investing public — has vastly increased. Indeed, it has increased to such an extent and is sometimes couched in such abstruse language (designed, no doubt, to convey technical accuracy) that much of it is comprehensible only to an expert in company financial analysis, while alternative treatments are still possible for many items of financial importance in assessing the likely fortunes of companies. At the very least, however, he would be able to express some gratification that Australia now is among the front runners in the setting of accounting standards.

Despite these changes it is nevertheless open to question whether there has been much progress in the essential problem facing accountants in this area, namely, the search for principles which express fundamental truths from which accountants can draw, with confident justification, the practices and procedures that they see to be necessary. Whether called "principles" or "conceptual framework", the security blanket has not yet been secured.

Even with the elaborate preparatory procedure, few, if any, standards as issued include reasoned, detailed discussion of

salient points, with argument for and against, before prescribing a practice under penalty of some kind of sanction for non-compliance. It will be suggested, no doubt, that the time and place for such argument is during the "due process", and especially when an exposure draft is issued for public discussion. This is accepted, but this phase does not provide for an exchange of views; it merely invites submissions which are not normally debated or discussed with the provider, but are taken into consideration by the processors. The practice in Australia, at least, is that the submitter eventually receives an acknowledgement and thanks for the submission. Thus, the standards present an appearance of ukase rather than "reasoning from sound principles". Perhaps we should not be too amazed at such an outcome from what seems to be more a politico-legal than a philosophico-scientific approach to the situations that accountants face.

If Fitzgerald were still available in the current environment, he would, of course, because of his eminence, be a prominent contributor to the standard-making process and no doubt he would be a member of at least one of the bodies involved in it; in this capacity he would bring his wide experience and strong influence to bear on the outcome. Whether that outcome to date would have been markedly different is purely speculative. The answer probably depends on whether the problem is, indeed, tractable or not, and this, in turn, depends on whether there are, in fact, any "fundamental truths" to be discovered in accounting theory or whether, in the last resort, there are only assumptions of human convenience and of limited applicability. This is a question still to be determined, if it is determinable at all: it remains a matter for the future, not the past.

*Louis Goldberg*

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