1967

Highlights: 1967 National Conference on Professional Ethics

American Institute of Certified Public Accountants. Committee on Professional Ethics

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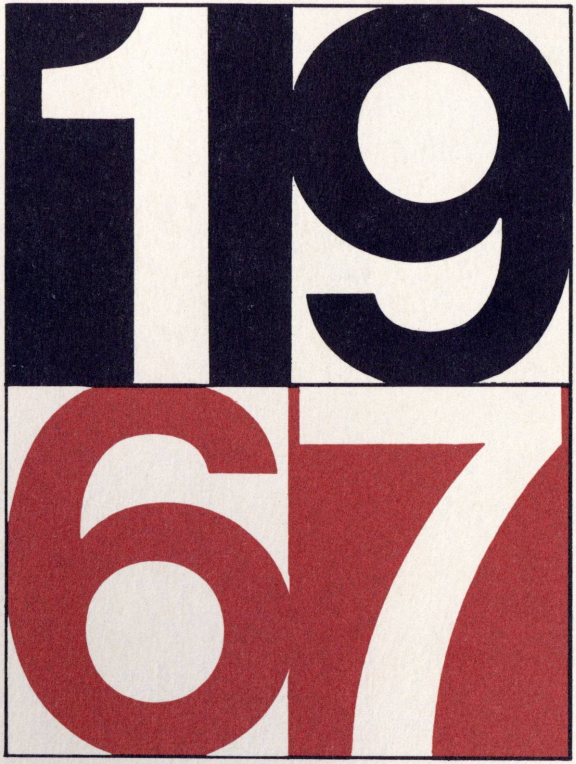

Committee on Professional Ethics *American Institute of Certified Public Accountants*

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Foreword

The Institute's committee on professional ethics sponsored the National Conference on Professional Ethics in New York on October 15-17, 1967, which brought together representatives of state boards of accountancy, state society presidents and executive secretaries, and representatives of state society ethics committees. The conference focused on attaining compliance with ethical standards.

The first session considered the reliance of the federal government on the work by CPAs and following talks by three government officials, the participants met in a number of individual discussion groups.

At the second session an executive secretary of a state society and state board of accountancy, and the staff assistant to the Institute's ethics committee and Trial Board examined the administration of ethical codes from their respective viewpoints. Following their talks, panelists again convened in individual discussion groups.

The third session consisted of a mock trial of a member alleged to have violated the Institute's Code.

At luncheon following the mock trial, Institute President Marvin L. Stone addressed the delegates.

The fourth session was devoted to a summation of the points raised in the discussion groups following the first two plenary sessions.

With the exception of the proceedings of the mock trial, this booklet includes the major addresses given at the conference. It includes also as an appendix the legal opinion regarding the exchange of disciplinary information requested by a delegate after the second session.

The committee on professional ethics wishes to express its sincere appreciation to Harry F. Reiss, Jr., chairman of the conference, to all the speakers who helped to generate discussion, to all the delegates who attended, and to the staff who worked so hard in planning and executing the conference.

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First Session

The Government Looks to the CPA

Fred B. Smith . . .

It is a special pleasure for me to participate in this conference today because the matter of professional ethics not only falls within the ambit of my responsibilities in the Treasury Department, but is also a matter of special personal concern to me.

I have a few thoughts that I would like to share with you, but I also want to take advantage of this conference, hopefully to get some ideas from you on how to deal with some difficult problem areas that are of mutual concern both to the Treasury Department and to practicing certified public accountants and attorneys.

Let me start by laying down a few initial premises. Some 70 million taxpayers annually file income tax returns under our self-assessment system, not to mention many other federal tax returns. Last year under this system we raised some $148 billion in taxes. The system is absolutely and utterly dependent upon the responsibility and honesty of the taxpayers in this country and their professional representatives.

As you know, until the enactment of the Agency Practice Act, we had in the Treasury a system of requiring special licenses for attorneys, certified public accountants and others to practice before the Treasury Department, and we had regulations which were very broad in their scope. In effect, we made a second judgment on a certified public accountant's competence and personal and moral qualifications to represent taxpayers before the Internal Revenue Service.

I was one of those in the government who led the fight in opposition to the bill which eventually became the Agency Practice Act. We opposed this bill solely out of our concern for the protection of the taxpayers and for the protection of the revenue of the United States.

Nevertheless, the act was passed, and, upon reflection, I am satisfied that we were wrong and the Congress was right in passing that act.

I am satisfied, that is, if, as I fully hope and expect, the state licensing authorities and the professional associations, such as yours, now assume and proceed to carry out faithfully the responsibility which the Congress has rightfully said is theirs, to maintain high standards of ethics and morality amongst their membership, and to weed out those disreputable and dishonest members who cannot be depended upon to live up to their high professional responsibilities.

In any event, the Agency Practice Act was passed and we drastically revised Treasury Department Circular 230, which constitutes the rules governing the practice of attorneys and agents before the Internal Revenue Service. The special licensing or admission requirement was, as you know, dispensed with. However, the act left in the hands of government agencies, including the Treasury Department, the authority to discipline attorneys, certified public accountants, and agents practicing before the Service for misconduct.

It was clear to us from the records of the hearings and the debates that Congress intended us to concern ourselves primarily with matters of misconduct relating more or less directly to the work of the Internal Revenue Service. Accordingly, the revised Circular 230 now sets forth standards of conduct, the violation of which would be the basis for suspension or disbarment, which fall principally into two categories: (1) those which more or less directly affect the right of taxpayers to sound representation before the Service, and (2) those which relate to the ability of the Service to carry out its functions and missions.

Let me give some examples of the kinds of things which might justify disciplinary action by the Treasury. If a practitioner willfully misrepresented facts to the Service with respect to his client's affairs, this would clearly be a matter of concern. Also, if he were guilty of willful tax fraud or evasion with respect to his own personal affairs, there would be serious doubt as to his qualifications to represent other taxpayers.

On the other hand, a great number of things that we used to consider in determining whether to grant a practitioner a license, or to discipline one admitted to practice before the Service, have now been eliminated. Some items *not* found in revised Circular 230 are: imparting to a client false information relative to the progress of a case or other proceeding before the Internal Revenue Service; improper retention of a fee for which no services were rendered; obtaining or attempting to obtain money or other things of value from a client or

other person by duress or by undue influence; endorsement of a government check drawn to the order of the client without authority of the client; and charging unreasonable fees.

The new provision on fees provides that the practitioner shall not charge an "unconscionable" fee. Under our interpretation, this means more than just charging a fee in excess of the professional association's accepted standards. We interpret it to mean an unscrupulous fee.

I think these examples will give you an idea of the new attitude which we now have with respect to the discipline of practitioners, and suggest the broad scope of the area of responsibility which we now regard as falling upon the state licensing authorities and the professional associations.

Since the enactment of the Agency Practice Act and the issuance of our revised Circular 230, we have heard from a great number of groups and individual practitioners, many of whom are somewhat overwhelmed and concerned with the situation that they have helped to create in supporting the enactment of the Agency Practice Act. This concern is to be found in the professional organizations and is particularly evident among those professionals who specialize in tax practice. They realize that the "bug is now on their backs," and they are not entirely happy to have this responsibility. As we have discovered over a great many years, it is not easy to police the membership of a profession. Those who serve on grievance committees perform the very delicate job of making initial judgments on the conduct of their fellow practitioners. In addition, the proper performance of this responsibility requires a great deal of time and effort on the part of very busy men. But I want to emphasize that, in my opinion, there are few undertakings which a professional man can perform which are more worthwhile. In the field of taxation alone, for example, practitioners are rendering a service which affects every taxpayer in the country practically, and in a vital way.

The integrity of our whole tax system is heavily dependent upon the ethical conduct of these representatives of the people. I am proud that, in my whole adult life, I have been engaged in the practice of an honorable profession. Although I am now in federal service, I may choose someday to return to private practice. In either capacity, the reputation of the profession to which I belong is a matter of great concern to me, and I know it is also to you. I realize that a few bad apples practicing among the legal profession can bring disrepute upon the profession as a whole, and I am sure you feel the same way about the practice of certified public accountancy. Both of these pro-

fessions have a very high reputation in this country today, but that reputation must be vigilantly maintained.

The Commissioner of Internal Revenue and I have both been the recipients of requests by professional associations for co-operation, particularly in the area of making available to state licensing authorities and professional associations derogatory information which comes to our attention. I can say without qualification that both of us are anxious to be of assistance in every way possible as you assume a greater proportion of the responsibility for maintaining the ethics of your profession. We have given quite a bit of thought to this matter, and we are engaged in studies looking toward appropriate avenues of assistance.

I am sorry to say that I cannot provide you with any very clear-cut conclusions at this point. Rather, as I indicated at the beginning of my statement, I am afraid that the most I can do is bring to your attention certain problem areas that have arisen in connection with our current thinking on this subject.

Let me take a relatively easy one first. Every year a certain number of disciplinary proceedings are initiated by the Director of Practice against practitioners for violation of the rules of conduct under Circular 230. Parenthetically, I might say that the Director of Practice is completely independent of the Internal Revenue Service, and organizationally is a part of the Office of the Secretary of the Treasury, operating under my general supervision. These proceedings are brought before an independent hearing examiner pursuant to the Administrative Procedure Act.

Evidence and testimony on the charges are heard and weighed by the examiner, who ultimately produces findings of fact and an order which may call for the disbarment or suspension from practice before the Service of a practitioner. We regularly publish in the Internal Revenue Bulletin the names and addresses of those who are disbarred or suspended as a result of such proceedings. However, the published notice does not give any details as to the nature of the violation. Query: Can a state licensing authority or professional grievance association take action against one of those members solely on the basis of a published notice of such a decision? It would seem to me that they might need more than this.

At the present time, I am exploring the question of how we can make available to appropriate bodies the findings of fact and order of the hearing examiner in this category of cases. One avenue to be explored is whether this can be done on the basis of requests under the Freedom of Information Act effective July 4, 1967. I am hopeful

that we will be able to work out a satisfactory system so that this can be done. There are problems with doing so, particularly in regard to professional associations, since from profession to profession and from state to state there are great variances in what you might call the legal standings and procedures of grievance committees. It may prove to be appropriate in some cases to recommend amendments of particular state laws to set up an adequate procedure for doing this.

There is a much broader area of adverse information which comes to the Treasury Department where the problem of co-operation with local authorities and professional associations is much more difficult. Many of these cases never go to a hearing before an examiner. After derogatory information is made known to a practitioner, he may consent to suspension, and that is the end of it. One might suggest that in such cases, guilt could be presumed and the adverse information and evidence which we have should also be made available to appropriate authorities. However, this may not be the case. A practitioner, in theory at least, might feel that he has such a small amount of tax work that he really doesn't care about being authorized to practice before the Service, and he doesn't want to go to the time, effort and expense to contest the charges and produce the evidence. In any event, there would not have been a production of all the evidence in a due process type of proceeding, a weighing of such evidence and a decision; and we have great difficulty at the moment in seeing our way clear to make this type of information available to local authorities under the circumstances—absent some statutory basis for doing so. This is an area concerning which I would be very interested to hear the comments and suggestions of any of those participating in this conference.

Finally, in the course of its review and investigation of tax matters all over the country, agents of the Internal Revenue Service may discover some derogatory information about practitioners, but this is derogatory information which does not relate to the matters encompassed by Circular 230. You might say it is accidental or incidental evidence and information which they acquire in carrying out their regular responsibilities. This is "raw" data which has not been tested, and we have great difficulty in seeing our way clear to making this type of information available to professional organizations. Bear in mind that, among other things, we are tremendously concerned not to cause any unfair harm to any individual practitioner. We are well aware that the disclosure of derogatory information which may ultimately be proved to be of absolutely no validity whatsoever can nevertheless do untold damage to the reputation of the practitioner. The

vindication almost never catches up with the publication of sensational charges and, of course, to a professional man, his reputation is his life blood.

I should like to touch on one further area which we are studying. Under our present regulations, flagrant misconduct by a practitioner before another agency of the federal government or, for that matter, state and local government, is not a basis for disciplinary action by the Treasury Department's Director of Practice. Nevertheless, we are well aware that an attorney or certified public accountant who files fraudulent statements with, for example, my colleague in the Securities and Exchange Commission, is certainly of dubious qualification to represent taxpayers before the Treasury's Internal Revenue Service.

Of course, the initial responsibility for coping with this type of incident lies with the other federal agency. But suppose a practitioner is disbarred from practice before the Securities and Exchange Commission. Some contend that this disbarment should be grounds for disbarment by the Treasury, but this can create problems. For example, I know of a similar case not involving Treasury's Director of Practice, but involving a Treasury license of a different sort. In this case, a man was denied a Treasury license on the basis of his having been found guilty of violations of an act administered by another department, resulting in the denial to him of certain privileges under that department's regulatory program. Subsequent to our action, this person provided the other department with additional information and evidence, and was reinstated and completely vindicated by the other department. We were considerably embarrassed by this incident because we had not held a proceeding in which an independent examiner had heard all of the evidence and come to a decision.

My tendency is to feel that while we can explore possibilities for co-operative arrangements among the various federal departments and agencies, essentially the task is going to devolve principally upon the state licensing authorities and the professional associations to keep track in the Federal Register and Internal Revenue Bulletin of decisions in disciplinary proceedings by the various departments and agencies, and to take the matter from there themselves. However, I will be very much interested to hear the views of my colleagues on the panel or of the other participants in this meeting on this difficult question.

These are a few rambling thoughts which I have, which I hope may make some contribution to the deliberations at this conference. We are very pleased that by and large our new Circular 230 has

found favor among the various professional associations. As you know, in the development of these regulations, we received great help in the form of suggestions from the various associations, and in particular, very thoughtful and constructive suggestions from the American Institute of Certified Public Accountants. It goes without saying that the Director of Practice and I, and I know the Commissioner of Internal Revenue, are always happy to discuss with representatives of your organization and other similar organizations any problems which may arise for you in connection with the way we carry out our responsibilities. And, as I have said, we are tremendously interested and anxious to be of whatever assistance we can in helping the various professional associations as they move into action to tighten up the quality and integrity of the services performed by their membership.

Discussion

Mr. George Nowak: Do you have any restrictive rules with respect to your Director of Practice?

For example, suppose a practitioner has gotten himself into difficulty with a client and he's brought up before the state board on charges. In the meantime, he's also having problems with Internal Revenue Service for failure to file his own tax returns and it's in the process of examination at the moment.

Now the board might check with the Director of Practice. Is there a written rule or restriction that might bid the Director to disclose information as to the status of the practitioner?

Mr. Smith: If I understand your question, I think you've hit one of the most difficult areas that we have.

When persons are in difficulty either with our Director of Practice or their own professional association, or with the state authorities, under the principle that we have in this country, a man is innocent until proved guilty. Therefore, we formally don't take any restrictive action with respect to that person's ability to represent clients before the Internal Revenue Service until there has been a completion of whatever proceedings are pending.

Of course, the representatives of the Internal Revenue Service are aware, frequently, of the fact that, let's say, charges have been made against a man and I suppose informally, they conduct themselves accordingly.

One of the most sensational situations is where a man is indicted

for bribery. When a CPA is indicated for bribery it may be two or three years before that case comes to trial and in the meantime, he's representing a lot of clients before the Internal Revenue Service.

We have found no solution to that problem.

I think you have a similar problem. What do you do about taking disciplinary action against a member of your association in similar circumstances? Do you wait until the trial has been held, or do you start proceedings right away?

One of the difficulties we have in the federal government is that to produce the evidence that we would need in the disciplinary proceeding might damage the criminal case, and therefore, the attorneys and Justice Department who are handling the criminal case understandably want us to go slow.

This is a very difficult problem area.

Mr. A. Leon Hebert: Do you have any problems imposed by the Spivak case, a disbarment case, here in New York where a CPA or practitioner might claim the Fifth Amendment in the disbarment proceedings themselves?

Mr. Smith: Yes, I suppose it would be a problem. I don't recall that this has actually happened in any of our disbarment proceedings. I don't recall that it has been done, but we certainly may run into that.

I don't know of any case. Of course, it's like everything else—you've got to get the evidence elsewhere if you can't get it from the man himself!

Speaker from the floor: May I ask what the position of the Bureau is with relation to a CPA who is called upon to defend or represent another CPA who's involved in an income tax violation and proceeds to clear the matter satisfactorily, but during the course of the engagement he becomes aware that his client has violated the profession's Code?

The CPA has a dual obligation.

First he has an obligation to his client; then, he has an obligation to society in terms of the ethical implications involved.

The man is sort of on the barrel or on the fence. Which way does he move?

Mr. Smith: Well, I think that living up to his obligations to his client with respect to privileged information would be his primary responsibility; that requirement in our regulations under disclosure would

have to be adapted to conform with what his obligations were to his client.

Does that answer your question? (Affirmative response). I think that would be our answer.

Philip A. Loomis, Jr....

The Securities and Exchange Commission has had a long and fruitful relationship with the accounting profession. Since I have had a relatively small part in that relationship, I am particularly glad to be here.

When the invitation came, I thought some mistake had probably been made and you really wanted Andrew Barr, our Chief Accountant, who has participated often in your deliberations and who, incidentally, among his other responsibilities, has primary staff responsibility for disciplinary matters involving accountants. However, I was told you really meant it, and I'm glad you did.

As I listened to Fred Smith, I could note very similar problems we have but also certain differences, both in our procedures and in our general approach, because accountants serve different purposes in relation to the Commission than they do in relation to the Treasury Department.

When Congress was considering, after the debacle of 1929, what could be done to provide protection for the investing public, one of the principal ideas first brought forward and embodied in the Securities Act of 1933 was the requirement of full and fair disclosure to the investing public. That has been the Commission's primary objective ever since.

When the '33 Act was pending before Congress, it was recognized that the scheme of disclosure with respect to securities depends upon accurate, informative and proper financial statements. It was also

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recognized that, unfortunately, people engaged in peddling securities, particularly dubious securities, cannot be relied upon to provide accurate financial statements themselves. It was consequently proposed that the government hire a corps of auditors who would go out and audit the financial statements that were to be filed with the Commission.

Largely for budgetary reasons, but also in recognition of the somewhat inappropriate nature of such a procedure, your profession came forward and suggested that the accounting profession would assume responsibility for auditing financial statements to be filed with the Commission. The Congress placed the responsibility on you by requiring that all financial statements filed under the Securities Act be audited by a public accountant or certified public accountant.

They did one other thing which is interesting: Schedule "A" of the Securities Act requires that all such financial statements be certified by an "independent" public accountant. Congress thus wrote into federal law the basic concept expressed in the Code of Professional Ethics of your profession that an accountant must be independent in his relations with his client. A great deal of the Commission's concern regarding accountants has revolved around the necessity for independence. The requirement, incidentally, was written into the 1934 Securities and Exchange Act, and into the Commission's rules thereunder.

If an accountant certifies a financial statement with the Commission when he is not, in fact, independent, that statement does not comply with the law and the Commission regards the certification as a nullity and the filing as defective.

Unlike the Treasury Department, the SEC has never had a separate bar or licensing scheme for attorneys or for accountants practicing before it. Rather, we allow practice to any person who is in good standing in the jurisdiction in which he resides. Again, that places the responsibility on the various state societies and boards. It's you, not us, who determine whether or not a person has the requisite qualifications.

However, we have had, since the very beginning, a disciplinary scheme for accountants and other professional people practicing before the Commission. This is codified in the Commission's Rules of Practice, Rule 2-E, and I think I might read it because it isn't too long:

> The Commission may deny, temporarily or permanently, the privilege of appearing or practicing before it in any way to any person who is found by the Commission after notice and opportunity for

> hearing in the matter (1) not to possess the requisite qualifications to represent others, or (2) to be lacking in character or integrity, or to have engaged in unethical or improper professional conduct.

This is pretty broad, and in practice we tend to narrow it a little.

We, like the Treasury, do not attempt to enforce all the standards of professional conduct that you have, particularly in regard to the relationships between the accountant and his client. We leave those aspects of professional behavior pretty much to the states. Our concern is primarily with our main job, which is to get adequate and accurate financial statements and to comply with the Congressional requirement that accountants be independent. Consequently, we have devoted our attention insofar as accountants are concerned primarily to three areas. First, was the accountant independent? Secondly, did the accountant follow generally accepted accounting principles, at least as he understood them? And, thirdly, did he observe generally accepted auditing standards? These matters relate to the quality of financial statements that are filed with us.

The Commission has a great deal of potential authority over accounting which, by and large, is not directly exercised. Section 19 of the Securities Act, which grants rule-making authority to the Commission, deals with financial statements in very broad terms. In part, it says:

> The Commission shall have authority to prescribe the form or forms in which required information shall be set forth, the items or details to be shown in the Balance Sheet and Earnings Statement and the methods to be followed in the preparation of accounts. . . .

Rather than attempting to prescribe systems of accounts or lay down generally accepted accounting principles by rules, the Commission, over the years, has co-operated with the accounting profession in the development of those principles. Occasionally, we have nudged you. Occasionally, you have nudged us, and I think, on balance, the result has been the continual raising of accounting standards.

Once accounting principles are generally accepted—and I understand there is some controversy every now and again in this area—the Commission expects practitioners to adhere to them. We also expect practitioners to adhere to generally accepted auditing standards.

In the area of independence however the Commission has reserved the right to establish its own standards. It has done so through issuance of Accounting Series Releases and opinions of the Commission. These seem to fall into three main areas:

First, there is the question of a prophylactic rule. An accountant for our purposes simply is not treated as independent if he has a

financial interest in the client, or any of the client's affiliates—even a rather small financial interest—or if he serves the client as an officer, director, or employee.

The second area with which we have been concerned involves the accountant who, in addition to doing the audit himself or through his employees, takes over some of the bookkeeping for the client just because that would be handy. By and large, we have endeavored, in co-operation with the profession, to discourage that. An auditor should not sit in judgment on what he or his associates did.

Finally—and here the concept of independence tends to merge with generally accepted accounting standards—there is the case of the accountant who subordinates his judgment to his client and does something that his client wants him to do, even though the accountant himself is not wholly satisfied that this is good accounting. We regard this in itself as evidence of lack of independence. If the accountant falsifies a financial statement in order to get it through in the form his client wants, we are satisfied that he is not, in fact, independent.

Thus, in our practice, the requirement of good accounting tends to merge in a way with the requirement of independence. We say that an accountant who is guilty of deliberate misconduct in order to oblige a client is not independent.

We turn now from the substance to the procedure. Although we don't require additional licensing, we do have procedures in our Rules of Practice for formally disciplining practitioners, be they accountants or lawyers.

However, probably the most common type of Commission proceeding involving the propriety of the accounting treatment in a particular filing is not in a disciplinary proceeding against the accountant.

At least initially, it is rather a formal administrative proceeding provided for by statute—either an investigation or a so-called "stop order" proceeding, or both. It is conducted in order to determine whether a financial statement was in fact false, misleading, or deficient, or failed to comply with generally accepted accounting principles, or whether generally accepted auditing standards were, in fact, observed.

If a financial statement is found deficient in any of those respects, it will be our view that the required accountant's certificate is false or misleading also, unless it reveals the deficiencies in the registrant's accounting. The accountant, therefore, may well be in fact, if not in theory, a sort of co-respondent in this type of case.

If we think the accountant was really culpable, such a case might well be followed by a disciplinary proceeding against him.

As in the Treasury Department, a disciplinary proceeding against

an accountant is commenced only by order of the full Commission, and almost invariably on recommendation of our Chief Accountant. It is heard before an independent trial examiner, under the Administrative Procedure Act in the same way as any other administrative proceeding before the Commission. Our office gets into it in that we provide trial services.

It has been our practice for years to make the records in those proceedings available to appropriate state authorities when they are completed. In fact, on occasion, we volunteer them by calling the matter to the attention of the state authorities for whatever use they wish to make of it.

However, as in the case of the Treasury Department, sometimes accountants do not want to fight; this is particularly true of people who have a very limited practice before the Commission. Perhaps it's the first time they're coming in and perhaps that's why they get into trouble. They simply don't know the rules.

In such situations, if we conclude that the accountant is culpable and something should be done about him, we will quite frequently dispose of the matter either by a suspension or resignation with his consent.

We do not reprimand. For some reason we've never gotten into that business. Either we don't do anything, or we write an opinion (which in a way is a reprimand), and if there are mitigating circumstances, let him off; or we suspend or revoke or disbar; and we accept voluntary resignations when circumstances warrant.

When that occurs, all that is usually involved is the signing of a short statement on which the accountant concedes the charges and resigns from practice before the Commission, or agrees not to practice for a specified period. This presents the same problem that Mr. Smith was confronted with. Such information is not very useful to the state authorities.

It doesn't mean, however, that we don't think the man is culpable. There is infinite variety in these situations, but if a man who has done a pretty bad thing which would justify his disbarment wants to resign, we generally let him do so in order to save him and us the time and expense of a formal proceeding. Therefore, it can't be assumed that merely because a man avoids discipline by consent, he was necessarily less culpable than a man disbarred after a formal proceeding.

Finally, we can refer cases involving accountants to the Department of Justice for criminal prosecution. This, fortunately, occurs very rarely, but generally I would say it would be done if we thought that an accountant was not merely practicing, doing his work, but

had conspired with his client in a scheme either to defraud or to file false financial statements with the Commission. Of course, this presents the same kind of problems that Mr. Smith has described: unless and until he is convicted, there are various obstacles to either your or our conducting a disciplinary proceeding against him.

Either we might hamper the Justice Department's prosecution, or the accountant might advance in our administrative proceeding the contention that he cannot testify and defend himself in our proceeding without waiving his privilege against self-incrimination in the criminal proceeding. Consequently, as a practical matter, the two proceedings cannot go forward at the same time. We have found this problem a difficult one. In affirming the conviction of an accountant and attorney who were acting as co-conspirators with their client in a fraudulent stock promotion, the United States Court of Appeals in New York highlighted the responsibilities of the accounting profession when it stated that:

> In our present complex society, the attorney's opinion and the accountant's certificate have become more lethal weapons for inflicting pecuniary loss than a kit of burglar's tools.

Our formal disciplinary proceedings, unlike our other formal administrative proceedings, are conducted privately until the hearing examiner's opinion comes down. This is done for the purpose of protecting the reputation of a man who might be able to show he was innocent, but means also that we have a problem in referring matters to you until they have been finally decided.

There's also another slight problem of liaison. We accept anyone who is licensed to practice in the jurisdiction where he resides, but we have to take his word for it. We can't go checking the rosters around the country to make sure that somebody who signs himself a certified public accountant in fact is one. There have been two or three cases where a fellow has signed such a certificate and it subsequently developed that he was not licensed to practice accounting anywhere.

On occasion, state boards have called such a situation to our attention if they observed it in the financial statements filed with us and publicized in our bulletins and we welcome that species of cooperation; otherwise we have no very good way of safeguarding ourselves against imposters.

In summary, the Commission and your profession have worked very closely together to raise accounting standards through insistence on adherence to proper practices and independence in the preparation of the financial statements. These are the major elements of what

has been conceded to be the world's most successful system of investor protection.

Discussion

Speaker from the floor: Mr. Loomis, have there been any criminal indictments of certified public accountants under the 1933 Act in which the accountant was not the specific object of referral by the Commission to the Department of Justice?

Mr. Loomis: I don't know whether you intended to limit that question just to the '33 Act, which I think might be a little beside the point. I believe there have been such indictments which resulted from investigations by grand juries rather than by us. On the other hand, I don't know of any such case which has occurred over our objections.

Speaker from the floor: Mr. Loomis, is the SEC able to submit to a state board or society its evidence against a practitioner who resigns from practice without admitting his guilt?

Mr. Loomis: I would think we should be able to do that, particularly if the state board or society requested the information.

Speaker from the floor: Mr. Loomis suggested that it would be desirable that information concerning a voluntary resignation from practice under the SEC could be forwarded to the state ethics committee or state boards of accounting. How would we know that such a circumstance occurred so that we might ask for it?

Mr. Loomis: I believe almost invariably, if not invariably, such resignations are the subject of a brief announcement by the Commission, copies of which go to the American Institute and to those people who have asked for them.

I think maybe there was some discussion of this in one of the group sessions, that state authorities can either establish direct contact with the Commission's Chief Accountant's office, or go through the Institute—whichever way they wish to do it.

Leslie Surginer . . .

We have assembled to study ways and means of maintaining the high ethical standards established for that segment of the public accounting profession represented by certified public accountants. It has been suggested that the excellent public image that the profession has so laboriously established now seems on the way to becoming slightly tarnished. If this is true, it is high time we became concerned and exerted every effort to protect it.

I am glad to have the opportunity to share with you the experience of the Rural Electrification Administration in utilizing the reports prepared by the public accounting profession. We have found them most useful in carrying out our program of responsibilities.

I believe you can best understand the degree of reliance my agency places on the high ethical and technical standards of the accounting practitioner if I briefly outline the program objectives of the REA and describe its use of opinion reports in meeting these objectives.

The Rural Electrification Administration is a lending agency in the United States Department of Agriculture. It makes self-liquidating loans to bring central station electric service, on a continuing basis, to unserved persons in rural areas and to extend or improve telephone service in rural areas. The REA was created by executive order in 1935 and was given continuing statutory authority one year later by passage of the Rural Electrification Act of 1936. The authority to make loans for the extension and improvement of rural telephone service came in 1949 with an amendment to the Act.

These two lending programs comprise the major operating programs of the Rural Electrification Administration. Electrification loans are made primarily to co-operative associations formed solely for the purpose of supplying electricity in rural areas; some loans are

made to power districts and municipalities and some to commercial utilities. About 60 per cent of our telephone loans are to stock companies and 40 per cent to co-operative associations.

Another category of loan finances the wiring of rural residences and the acquisition and installation of electrical and plumbing appliances and equipment, including electrically-powered commercial machinery, by power consumers. In no case is a loan ever made directly to the consumer; the funds are advanced to system operators for relending to their members. The REA's creditor relationship thus remains with the system operator.

Electric and telephone construction loans are self-liquidating within a period not to exceed 35 years, while residential wiring and appliance loans are made for a shorter period. There are loans outstanding in every section of the continental United States, including Alaska and Puerto Rico. Our borrowers serve more than 20 million rural people.

The REA has made loans of $6.6 billion since the inception of the program. Of this amount, more than $1.9 billion has been lent during the last six years. The unpaid balance of loans outstanding at September 30, 1967 was about $4.6 billion. Interest and principal past due at that date was $2.5 million. Of this delinquency, $2 million involves a legal situation. We have had to charge off less than $50,000 since the inception of the program.

The rural electrification and telephone programs have had an ever-widening effect on the nation's welfare. Early in the 1930's, with the breakthrough of rural electrification, the general public viewed this program primarily as a provider of light to the long-darkened rural vastness of America. Later came the understanding of what it means in terms of more efficient and productive farming. Now we are concerned with the potential for diversified economic development and the part these programs will play in creating the rural-urban balance required for the future of the country.

Fortunately for these basic programs, the Rural Electrification Administration has always been staffed with people of vision and dedication. Its mission seems to attract individuals imbued with a strong desire to help others help themselves. REA representatives have worked with local groups toward organization of local electric and telephone co-operatives and have assisted small rundown stock companies to take steps required to provide better telephone services. In these activities the REA frequently has financed up to 100 per cent of the cost of constructing a system, then helped many of the groups in the operation of their system by furnishing management, accounting and engineering assistance.

The REA has about 900 employees, including 200 field personnel. Its relations with borrowers are centralized in REA's offices in Washington, D.C. We have no regional or field offices. Field employees, who work directly with borrowers, are headquartered in their homes and report to their Washington supervisors.

In the early years, as a measure of loan security, REA auditors periodically audited the books and records of each borrower. From the very beginning, these auditors were interested in more than the borrower's financial position at a given date and operating results for a stated period. Their stay at a borrower's office, frequently three or more weeks, gave them the insight into its day-to-day operating practices as well as a basis for forming an opinion as to its financial condition. The broad knowledge of borrower operating practices enabled REA staff auditors to give timely assistance in many areas besides accounting.

After World War II, suggestions were made from time to time that borrowers in sound financial condition could be asked to assume responsibility for the audits of their records. In December 1947 the REA wrote to all borrowers having a net worth equal to 25 per cent or more of assets and having lines which had been in service five years or more, requesting them to provide for annual audits by certified public accountants approved by the REA. At that time 81 borrowers qualified under the new policy and were required to provide independent audits.

The program of independent audits by certified public accountants has expanded each year until now all electric and telephone borrowers are required to provide independent audits, except for a few considered to be potential loan security risks. Currently, 1,784 of the total of 1,839 active borrowers have their annual audits made by certified public accountants. They use the services of more than 500 different firms and individual practitioners. This includes around 300 firms or practitioners who do only one audit. The size of these firms ranges from a single practitioner to members of the so-called "Big Eight." Through the fine co-operation of most of the certified public accountants making the audits for REA borrowers, the entire independent auditing program has proved very successful.

A typical mortgage agreement under which electrification and telephone loans are made requires the borrower to furnish within 30 days after the close of each fiscal year a full and complete report of its financial condition as of the end of such fiscal year, the report to be certified by its treasurer and, if so requested by the REA, audited and having an expression of opinion of an independent public accountant satisfactory to the agency. As a matter of actual prac-

tice, the REA requires its borrowers to have their accounts and supporting records audited annually by independent certified public accountants selected by the borrower and approved by the REA. These annual audits, together with a long-form report prepared in accordance with minimum standards established by the REA, are accepted as meeting the various mortgage requirements relating to a full and complete annual report.

The Rural Electrification Administration has consistently held to its requirement that the auditor must be a certified public accountant. Although there are many uncertified practitioners who are fully qualified, the REA has no means for examining their qualifications, whereas a certified public accountant is required to meet state-prescribed requirements and standards to receive his certificate and is expected to maintain the standards established by his profession in order to retain his certificate. It is expected further that he will comply with the rules and regulations of the states in which he conducts audits and prepares audit reports. We place great reliance on state boards of accountancy and state societies to see that proper levels of ethical conduct and technical performances are maintained.

Since the certified public accountant is selected by the borrower's board of directors, subject to approval by the Rural Electrification Administration, the basic relationship is between the borrower and the auditor. As mortgage-holder, the REA requires that it be furnished copies of the audit reports for its information and use. If requested, the independent auditor's working papers are to be made available to the REA. For obvious reasons, the auditor must be completely independent of management in the performance of his auditing and reporting.

The REA has provided each of its borrowers and each certified public accountant performing audits for borrowers with a comprehensive bulletin setting forth minimum requirements as to audit procedures and expected disclosure. This policy bulletin on auditing requirements provides for an extensive examination of the accounts, and requires a report that includes specified information beyond that ordinarily furnished in the conventional long-form report. In addition to the balance sheet, income and expense statement, and statement of margins or surplus, the independent auditor must furnish detailed information concerning each balance sheet item, statements relating to the condition of the accounting records, and comments concerning his evaluation of the internal control procedures in effect. Although very important for management purposes, a statement of source and application of funds is not required at this time by the REA for credit supervision.

The auditor is expected to make every reasonable effort to eliminate deficiencies or furnish recommendations to the client for eliminating or improving existing conditions. If an irregularity in the accounting records or practices (defalcation, fraud, or false reporting, for example) is disclosed during the audit, the auditor is expected to notify immediately the borrower's board chairman and the REA.

The rather comprehensive information prescribed by the REA for inclusion in audit reports is considered necessary because of the low minimum equity required of its borrowers. The agency is interested in more than an opinion on financial position, important though that opinion is. Since changes in financial position are a matter of history, the REA is particularly interested in operational aspects indicative of trouble ahead which, through prompt action, may be eliminated before becoming a matter of history.

As I indicated earlier, our program of requiring borrowers to provide for independent audits has proved generally satisfactory. We do, however, have some problems.

Probably the foremost of these has been the reluctance of some public accountants to follow the minimum requirements for auditing and reporting prescribed by the REA. Sometimes, in the interest of keeping down costs, the borrowers themselves have limited the extent of the audit or the scope of the report. In other cases, however, the reports submitted have omitted data of importance either because the auditor felt it was not necessary or he was not well informed as to the requirements. Another possibility is that he was unwilling to do the auditing necessary to enable him to make the prescribed comments.

Although we have no proof of this assumption, we suspect fees have a direct impact on the quality of the work. We have found frequently that, when fees are low, the quality of the work is poor. We feel that the whole question of how fees are determined deserves considerable attention by the state boards and societies.

Another problem of concern arises when the certified public accountant auditing the borrower's records is unfamiliar with the utility accounting applicable to the electric or telephone system he is auditing. In some cases, the unique features of the corporate structure of the co-operative organizations are disregarded. Although a number of accounting firms have specialized in these audits, and have familiarized themselves with the required auditing and reporting standards, a few practitioners who perform audits for one or two borrowers have not taken the trouble to become conversant with the special standards applicable to the utility being audited. All too frequently independent auditors have made recommendations which

have been in conflict with the prescribed uniform system of accounts and recommendations of the REA.

It is of grave concern to us when certified public accountants make recommendations contrary to the REA's prescribed uniform system of accounts and its published policy bulletins. It creates a problem for the agency, for its borrower, and eventually for the accountant. In making such recommendations, it seems the accountant has to make a razor-edge distinction between his independence, his responsibility to his client, and to a very much interested third party. Somehow it doesn't seem prudent for the accountant to be in the position of fomenting trouble between his client and his client's source of financing.

A final problem of importance is lack of disclosure, particularly in cases of mortgage violations and lack of internal control. It is not always clear whether the failure to make required disclosure is due to an oversight or is linked to lack of independence. In common with most lenders, the REA has written into its mortgage agreements restrictions requiring reservation of earned surplus and limiting the payment of dividends or patronage capital refunds until the borrower has attained a specified financial status. The independent auditor is expected to familiarize himself with the provisions of the mortgage agreement and by his examination to determine whether they are being observed. Likewise, many borrowers have in their bylaws a plan for handling patronage capital which is in effect a contract with their consumers or their subscribers. The REA is greatly concerned with the proper observance of these requirements and expects the audit report it receives to provide information on any noncompliance. In too many instances we also find apparent reluctance to disclose weakness in internal control, particularly as it relates to the handling of travel and miscellaneous expenses of the management and board of directors.

This disclosure problem brings into focus a very serious issue—which might not be limited to reports filed with us. There seems to be a lack of feeling of real responsibility to third parties on the part of too many public accountants. Occasionally, through some channel other than the audit report, the REA finds that a borrower has violated the provision of its mortgage or bylaws, or both. In a few cases, borrowers have used subterfuge, such as the payment of unreasonable salaries or bonuses to officers or owners, in order to bypass dividend restrictions. When these and similar violations are not disclosed in the audit report, the accountant is not complying with the spirit of his professional standards requiring full and complete disclosure to third parties. This is particularly serious when, as in our case, the third party is readily identifiable and its interests are, or should be, known to the auditor.

In the interest of overcoming deficiencies which mar an otherwise excellent program, the REA endeavors to work with its borrowers and the accounting profession to improve the quality and reliability of audit reports. It has a small staff in Washington reviewing all audit reports received, to ascertain that each audit report substantially meets the requirements set forth in REA policy bulletins. Where it is pertinent, the borrower and the certifying accountant are advised of reporting deficiencies and suggestions are made for improving future audit reports.

This office review is supplemented by an evaluation at a later date by REA field accountants. Our field accountants, in connection with their periodic examination of borrowers' records to ascertain that loan funds have been used for the purposes for which the loan was made and to observe any practices contrary to program objectives, are asked to comment on such matters as:

1. Are the independent auditor's statements about internal control factual?
2. Are recommendations to the borrower consistent with Rural Electrification Administration policy and procedures?
3. Were any major violations of the mortgage or loan agreement observed which were not disclosed in the audit report?
4. Did the scanning of the books of original entry reveal any basic accounting errors which were not disclosed by the independent auditor?
5. Were the independent auditor's statements relative to plant accounting factual and complete?
6. Were errors or omissions noted which would have changed the financial statements or the audit report to a substantial degree?

We recognize this review is not comprehensive and lacks depth. The REA purposely avoids duplicating the work of the independent auditor and does not audit behind him, but the answers to these questions do touch on key points and provide some basis for evaluating the quality of the work being performed.

In selected cases, the working papers of the public accountant are examined. This is the only way we can determine whether a proper audit has been performed or not. We have been disappointed in many of the papers reviewed. However, we believe that most practitioners have a sincere desire to improve their work and, through a cooperative approach to this matter, progress is being made.

If substandard auditing is indicated, the agency may revoke its approval of the certified public accountant to perform further audits for any of its borrowers. Or it may, if the circumstances seem to

justify some leniency, place the auditor on probation and subject his reports and working papers to close scrutiny for a period of time. If, at the end of the probationary period, the REA is satisfied that the audit performance meets acceptable standards, including all of the agency's prescribed requirements, full approval is restored. If not, the REA has no choice but to revoke approval for any further audits of borrowers' records.

I have briefly outlined the experience of my agency in utilizing the reports of certified public accountants and the great degree of reliance we place on the high ethical and technical standards of the accounting profession.

I have also briefly discussed the remedies we have for sub-standard work. In the final analysis, however, the real responsibility for maintaining standards is yours. So far as I know, we are the only federal agency which has pegged its reporting standards at the certified public accountant level. We have been able to do this only on the premise that high technical and ethical standards are guaranteed by vigorous state boards of accountancy and equally zealous state and national organizations. Don't let us down!

In conclusion, let me say again, that the REA is generally well pleased with its program of reliance on independent audits in its administrative process. Clearly much of the success of the program is the result of the generally high qualities characteristic of the participating certified public accountants. In the main, they have been co-operative, interested in the objectives and progress of the program, and anxious to do a good job. Furthermore, since the program's inception, the American Institute of Certified Public Accountants has recognized our audit program's importance to the accounting profession and has actively cooperated with the REA in making it a success. The Institute's committee on relations with the federal government and the Institute's Washington division have been especially helpful. We are looking forward to this kind of continuing co-operation. We would like to establish an equally successful working arrangement with state organizations.

Discussion

Speaker from the floor: Mr. Surginer, you mentioned that your agency would like to refer disciplinary matters to the professional organizations for resolution rather than have them go through a full trial.

How would you expect such a system to work, and aren't there legal problems involved?

Mr. Surginer: When the problem is ignorance of required standards, I would prefer that we not go all the way to a disciplinary trial. I would rather work with the state boards in an educational framework and have some sort of discussion with the individual concerned.

I think this would provide a mutual assistance to the practitioner. It would certainly help us and benefit the public.

Speaker from the floor: Mr. Surginer, do you expect the borrower's auditor to inform the REA when he feels salaries are too high? Isn't this an improper burden to place on the CPA?

Mr. Surginer: What I have in mind is that the known documents provide, under certain circumstances, that the increase in salaries or any salary adjustments will be approved by the REA and what I have reference to here is disclosure of the fact when salaries have been increased contrary to that mortgage or loan provision.

In other words, I would not expect you to pass judgment on the propriety of the salary level. It's only the matter of the violation of the loan agreement.

Second Session

Attaining Compliance with Ethical Standards

William J. Caldwell, Jr....

I wish that I could offer some profound observations and some really down-to-earth solutions for obtaining compliance at the state level through the machinery of the state board and the state society. Because some of today's problems had their origin a number of years ago, let's make just a brief estimate of the situation.

Whether characterized as rules of professional conduct or codes of ethics, we're talking about guidelines of conduct voluntarily accepted by those entering the public accounting profession. The codes define conduct which will maintain high standards of technical competence, morality and integrity in the public interest.

I believe that it's an accepted fact that a code of ethics is one of the keystones of a professional person, equal in importance to formal education, demonstrated competence and public service.

But for many years a written code of ethics was not a part of public accounting. Only in very recent years has substantial nationwide uniformity in this area been established.

The first record I could find of a code of ethics being adopted was in the 1919 Yearbook of the American Institute. There were eleven or twelve rules. At that time, as you all know, there were very few certified public accountants in the United States.

I'm not familiar with the situation in other states, but in Kentucky the board of directors of the Kentucky society considered a code of ethics as early as 1936—and when I say early, that may seem early in the profession but it has been relatively recent. They did not adopt such a code at that time, but continued to function under the American Institute's Code until 1948 when they adopted their own. In 1946, immediately after the passage of Kentucky's first regulatory public accounting law, the Kentucky State Board of Accoun-

tancy adopted almost word for word the American Institute's Code.

This means that quite a number of CPAs in practice today entered the profession in Kentucky at a time when there were no codes of ethics governing their practice. And I'm sure this would be true in most other states.

I think that we can reasonably assume that those CPAs who were members of the American Institute or of a state society having a code may have been aware of the provisions of the code on entering the profession. However, I seriously doubt that very many have made an effort to study their complete significance or to keep abreast of subsequent changes. In addition, we should realize that there are today in the United States a number of CPAs who are not members of either a state society or the American Institute. These fall in a category of the "unreached" since they receive little or no communication from a professional organization of certified public accountants.

This latter group, of course, must be considered the sole responsibility of the licensing board.

As I see it, we in professional organizations who are concerned with compliance inherit the other segment of the profession, the "unconcerned" or "uninformed" or both.

Where do we stand today?

Since public interest is the basis for state laws licensing the public accounting profession, most of the state accountancy laws provide for state boards to promulgate rules of professional conduct. According to the latest tabulation from Commerce Clearing House, all but six states and the District of Columbia now have codes of ethics as a part of their regulations. These six states are Illinois, Indiana, Louisiana, Maine, Maryland and New Hampshire.

The AICPA Code, state society codes and those boards having rules of professional conduct are almost uniform throughout the United States and uniformity is a big step forward in that it eliminates state lines and promotes co-operative efforts in enforcement.

In my opinion, no CPA would want to be in public practice without rules governing his relationships with clients, colleagues and the public. If this observation is correct, then why do state societies and state boards have problems with compliance? There are two principal reasons: first, a lack of knowledge and understanding of the rules, and second, a lack of diligent enforcement.

Let's consider the first reason for a moment. There are no training courses concerned specifically with professional ethics. With the exception of areas touched upon in auditing courses in college, CPAs must gain their knowledge and understanding through the dissemina-

tion of information by a professional organization or by the state board of accountancy.

Those of us who are concerned with state society publications must assume some of the blame for failing to disseminate enough information on ethical matters. Of course, we can never be sure of our readership, but at least we could give the exposure that is needed.

For example, I'm sure most of you recall the article in the June '67 issue of *The CPA,* the Institute's membership bulletin, announcing that a member had been expelled from membership in the American Institute for publication of a card in a newspaper in the Bahamas. We wonder why this individual would not have known that this was a violation of the code of ethics and yet, about twice a year, I receive telephone calls from members of the Kentucky society who are planning to open an office or even relocate offices and they want to know what size card they can put in the paper!

To publish this type of disciplinary information certainly gets the problem across to members who read it and if there were any who were unaware of the rule against publication of a card, they should no longer be in doubt.

Unlike the Institute's CPA bulletin, which goes only to members, state society publications have a distribution to many outside the profession. This raises a question as to the advisability of publishing details of disciplinary actions in any publication going to the general public.

After preparing this talk, I looked through the clippings that came in through our clipping service and what did I find but an announcement or a card which had appeared in the paper in the Louisville area. I was amazed to find that we're not getting across to our members the fact that the card has been prohibited for a number of years. I just don't know how we can reach members who won't read what is sent to them.

During the planning stages of this conference, the American Institute requested of state societies and state boards information on disciplinary action taken during the period of January 1, 1962 to July 1, 1966.

Kentucky responded to this request and submitted forty instances of violations handled by the state board and twenty-one handled by the society. None of these disciplinary matters were publicized in any release to the membership or to the registrants of the state boards. I'm glad to say that most of these violations concern professional behavior rather than technical standards.

The Kentucky board is now studying the matter of releasing its

enforcement activities without the use of names, except in cases of revocation of certificate. This would be a means of indirectly educating members of the profession in ethical matters.

Progress is being made in education in ethics, both by state boards and state societies. A growing number of state boards of accountancy require examinations in ethics before the issuance of a certificate. In that connection, the National Association of State Boards of Accountancy supplies questions on ethics from their stockpile for the use of state boards. With some twenty state boards giving their own ethics exams, the Board of Examiners of the American Institute now limits ethics questions on the CPA examination to those affecting auditing and reporting standards as distinguished from ethical behavior.

More and more state societies are publishing codes of ethics in their membership directories and other publications. Some few, from time to time, publish interpretative opinions in their bulletins and some state societies are trying to make effective the AICPA proposed program of practice review. In addition to these, the AICPA staff training program has a session on ethics and some firms—and I hope there are many—hold staff sessions on ethical standards. These are several of the avenues by which members of the profession become knowledgeable in the area of ethics.

A thorough knowledge and understanding of the code provisions should be a primary goal of state societies and state boards.

Now, let's look at the other reason creating a problem in compliance—lack of diligent enforcement. Who is at fault? State society ethics committee? Trial Board? State board? Members? Certainly all are to blame to a certain extent.

Diligent enforcement requires first of all that members be aware of what constitutes a violation and, second, that they be willing to report to the proper authority. Diligent enforcement also connotes prompt action, and problems arise in this area. Unfortunately, members are reluctant to assist in this policing activity.

Ethics committees of state societies too often are slow to act. State boards meet infrequently and their formal hearings require detailed arrangements. And there's a hesitancy to publicize violations of members.

When we talk of members' reporting violations, I'm sure that many of you, particularly those concerned with state board activities and society management, receive the same verbal complaints that I received with regularity. These are oral reports of violations of technical standards from a CPA who follows another on an audit. Others

call to report that some firm or individual has solicited one or more of his clients.

Are these members willing to register a formal complaint in writing and where necessary, submit documentary evidence? No! In the first instance, the client would have to be brought into it and would become involved and that would not be good for client relations. Also, the CPA who preceded him on the job would be pretty sure where the complaint came from and this, it is felt, would not be good for professional relations. In the second instance, the CPA who is charged with solicitation usually has been unable to take the client, so in the complainant's reasoning, no damage has been done.

No formal complaints are filed. In each instance, they are just passing along the information to me so I can drop a note in the file for future reference. Are these members at fault for not filing a formal complaint?

I would have to agree with the remarks that John Lawler made in his report to Council in Portland when he said:

> The CPA who refrains from disclosing the misconduct of another CPA, particularly when that misconduct could now or later adversely affect the interest of others, might well be considered to share in the guilt of the errant member. As a matter of fact, he might be even more guilty, for some of the undetected sins of omission or commission may be products of ignorance rather than of design and will be repeated if not promptly discovered, to the injury of the public welfare, the offender's reputation and the profession's prestige.

Overcoming this reluctance is going to take time. Ethics committees, by prompt action on reported violations, can help remove this reluctance.

I know of instances where violations have been reported and because of the delay in investigation and failure to take action, the CPA who reported the violation came to the conclusion that it did no good to report violations since it appeared that nobody would do anything about it. This problem can be removed by proper selection of ethics committees and speedy handling of alleged violations.

There is, too, the problem facing state boards of accountancy who meet infrequently and whose hearings require detailed arrangements. At the present time, very few state boards have the personnel required to make investigations of complaints for the simple reason that funds are not available.

Many accountancy laws did not envision all the administrative functions that have fallen to state boards. Very often, to obtain these

funds, the boards must petition the legislature in their respective states. This can be changed but it will not be done until state boards recognize their responsibility and seek to provide the funds necessary for enforcement.

From the comments I've made thus far, you might get the impression that I do not believe that progress is being made in enforcement. This is not so. In the twelve years that I have served the state board and the Kentucky society, I have witnessed a great deal of progress, not just in Kentucky but in other states. State societies are focusing greater attention on prompt and fair enforcement and state boards of accountancy are focusing on the educational aspects, as well as enforcement.

While I know that we in Kentucky are not doing everything we should, some of you may be able to profit from the preventive steps we are taking.

First, the State Board of Accountancy requires an examination on the code of ethics as a basic part of every application for examination or certificate by waiver. This is an open book examination and all examinations are graded. Any incorrect answer is called to the applicant's attention by letter.

Second, all successful candidates are required to attend a briefing session on ethics with the State Board of Accountancy and members of the society's ethics committee. This session is held on the day that the new CPAs are to receive their certificates. During the briefing session, they are presented with a copy of the AICPA publication, *Ethical Standards of the Accounting Profession.*

The most common violations coming to the attention of the board and several of the numbered Opinions and informal opinions are referred to and discussed. In Kentucky, the candidate has to have completed the experience requirement before he sits for the examination. This makes it possible to discuss practical applications of the rules which might be difficult in states which issue the certificate before experience is completed.

We urge all new CPAs when in doubt about possible ethical considerations of any contemplated act to call the state board or society office and seek advice before possibly committing a violation. We also urge them to report any violations that come to their attention and we place the responsibility for assisting in the policing of the profession squarely upon the new CPA. We assure them that the source of the complaint will not be revealed unless subsequent events prove that he must be brought into it.

Third, every person receiving a certificate is required to take the oath of a CPA in which he swears to abide by the rules of profes-

sional conduct and sign his name in the oath book. We also subscribe to a clipping service. This has proved to be a source of information on violations by members of the profession.

We require that all complaints of violations be in writing. If the alleged violator is a member of the Kentucky society, the ethics committee receives the complaint immediately. If he is not a member of the state society, the state board investigates and disposes of the matter.

When, in the opinion of the Society's ethics committee, the matter is serious enough, its findings are turned over to the state board. The matter is then disposed of in either an informal or a formal hearing. I might add that the American Institute is also informed.

You will recall that President Giffen last February urged the exchange of information on ethical matters between the American Institute and state societies and state boards.

The Kentucky board immediately requested an opinion from the Attorney General, who ruled as follows:

> Judgments of the board as to violations of the code of ethics, reached after investigation and hearing, are not confidential but represent a public record of a state agency acting in the public interest. There is no reason why findings of the board that licensees have violated the code of ethics should be withheld from such interested organizations as the Kentucky Society of CPAs or the American Institute of Certified Public Accountants. Release of information as to violations could, in fact, have a salutory effect upon the profession.

Enforcement is not a simple task, nor a pleasant one. No society ethics committee and no state board relishes sitting in judgment on a fellow practitioner for a violation of the rules of professional conduct, but it must be done. And it goes without saying that no CPA wants to be called before a society ethics committee and certainly not before the state board for any reason.

To promote compliance, we must reduce the incidence of violations. To accomplish this, we must rely upon education, examination and information.

First, we must educate through ethics courses in colleges of accounting, and I mean a more specific course than is now given by professors in auditing courses; through staff training courses, both formal and informal; by precept and example of senior members of the profession; through written examinations on ethics before the issuance of a certificate; by informative programs at state society

annual meetings and chapter meetings; and by information releases through state society publications and state board bulletins.

Second, by diligent enforcement through a society ethics committee of seasoned members whose integrity and professional standing is unquestioned; by encouraging members to help police the profession by reporting violations, even minor ones and doing so promptly; by handling complaints promptly and by publicizing the activities of the committee in newsletters or special bulletins to members, we can also reduce the incidence of violations.

One of the goals of this conference is to determine how to obtain compliance with the provisions of the code of ethics. I hope that my remarks may prove helpful to some of you in reaching this goal.

Discussion

Mr. George Nowak: I wonder if Mr. Caldwell would elaborate a little further on the ethics examination. When do they give it? How long? Who grades the exams?

Mr. Caldwell: The ethics examination is a series of questions requiring the applicant to review the entire code of ethics in order to be able to answer the questions properly.

The examination must be in his own handwriting on a prescribed type of paper. It is submitted at the time that the application is submitted and I review the answers and then submit the examination together with the rest of the application to the members of the board.

If there are any comments on the answers that may be given on the examination and it's necessary to call it to the attention of the applicant, then I'm the one who usually writes the letter.

There are fifty questions on the particular examination that we give. Of course, the examination is revised from time to time. It's given ninety days before the month of the CPA exam.

Speaker from the floor: Willard Bowen who was in charge of the committee which set up the exams for the Association of State Boards of Accountancy is here.

Chairman Reiss: Would you like to add something to what Mr. Caldwell said?

Mr. Willard Bowen: The recommendations of the National Association

of State Boards of Accountancy can be obtained by every state just by writing to the National Association of State Boards of Accountancy.

Our committee has set out a complete set of recommendations for giving these examinations and we have a committee on examinations sending out a set of questions and answers, at least once a year, for the use of all the state boards. Open book ethics examinations are readily available to any state board and I highly recommend that the boards who don't have them now consider adopting them.

Donald J. Schneeman . . .

When we talk about administration of a Code of Professional Ethics from a national point of view, three questions seem particularly deserving of our consideration:

First, is there sufficient awareness of professional ethics and concern for its enforcement among practitioners?

Second, is there adequate machinery for enforcement at the state board, state society and Institute levels?

Third, is there adequate exchange of information regarding disciplinary matters among all of these interested jurisdictions?

Let's look at the last problem first, the exchange of information regarding disciplinary matters.

In February of this year, Institute President Hilliard Giffen wrote to all state boards of accountancy and CPA societies expressing his concern over the status of the profession's disciplinary efforts. There has been a growing concern about this among Institute presidents in the recent past, and the issuance last year of the new Treasury Circular 230 served to bring things to a head.

As you know, the Internal Revenue Service has abandoned a very large part of its disciplinary effort as far as CPAs and lawyers are concerned. Gone is the Treasury card and gone is the agency's right to revoke or suspend it. The sole criteria for practice by CPAs before the IRS now is possession of a valid CPA certificate.

This appears wholly reasonable. If the accounting profession is self-disciplining, there is really no need for the federal government to perform a duplicating disciplinary role.

One reason for the Treasury's willingness to restrict its disciplinary activities may well have been the inherent difficulty in policing the activities of all Treasury card holders by a single agency. The

decentralization of responsibility to the state level therefore seems a very good thing for all concerned. However, those who are familiar with the disciplinary activities of state boards and societies and of the Institute may well ask if the profession is prepared to accept this challenge.

One indication that it may not be is the lack of uniformity in codes of ethics, but this is less of a problem as time goes on and codes become more uniform from jurisdiction to jurisdiction.

Another indication is the difference in interpretation of similar rules by different bodies and the disparity in penalties meted out by various disciplinary authorities for similar offenses. As an example, the Institute is informed that some of its members who have been expelled by the Institute after having been convicted of felonies, have retained their CPA certificates in full force and effect. It could be argued that this results from local considerations.

At one time, it may have been a matter of only local concern when a state board restricted the right of a person convicted of a serious crime to practice as a CPA. Under the old Circular 230, the status of the CPA certificate was probably of minor concern to the Treasury when it could fulfill its public trust by revoking the practitioner's Treasury card. But the situation is completely different now that a person can practice before the IRS simply by showing that he has a valid CPA certificate.

The almost total reliance of the Treasury Department on the integrity of the CPA certificate places a heavy responsibility on state boards to enforce standards of conduct and discipline CPAs who violate ethical standards or who are convicted of serious crimes. And as Les Surginer pointed out this morning, the same principle applies to agencies which, like the REA, accept the CPA certificate as qualifying a person to practice before them.

But it has been truly said that we do not improve the ethics of the profession by drumming out convicts. A person who has been convicted of a serious crime is probably the easiest to discipline because the courts and usually a jury have found that his behavior has fallen below the standards set by society. In a sense, someone else has made up our minds for us.

The case of the practitioner who appears to have performed substandard work presents the profession with a far more difficult, but infinitely more significant problem. First, was he simply negligent, or has his practice been characterized by substandard work? If the latter, is it because he is basically a bad operator, or is it simply that he's ignorant of the profession's high standards of competence? If he

does not know the technical standards, are our educational efforts and standards to measure minimum competence through the uniform CPA exam adequate?

And if we're sure that the practitioner entering the profession has adequately proved his basic competence through the exam, why did he later lose contact with the technical standards? Is the profession's program for continuing education adequate in this regard? Have we failed in our obligation to encourage and perhaps even force him to maintain his proficiency?

These are questions which should and must be considered in any matter coming before an ethics committee or Trial Board dealing with technical noncompliance.

We must analyze how we should deal with his failures. Does a suspension from practice as a CPA or from membership in a professional society for failure to observe technical standards carry with it the obligation that before the suspension is lifted, the member must prove to the satisfaction of the disciplining agency that he understands his technical deficiencies and has educated himself so that the offense will not happen again? Is such a procedure practical or desirable?

Until we reach the utopia of a single disciplining authority, any disciplinary authority should be able to feel that the integrity of its decisions will be respected to the extent that action by one such authority will cause the other authorities to initiate an investigation.

For example, the SEC should be able to feel confident that all professional bodies regularly review accounting series releases, so that when it is shown that a practitioner has failed to comply with accounting standards, the boards and societies concerned will initiate an investigation which might lead to disciplinary action by those groups.

In some cases, the SEC will accept a resignation from practice in lieu of a formal hearing before the Commission and will publish its findings. Often these releases suggest to a reader that the profession's technical standards have not been observed by the party concerned. While the Commission's powers end with acceptance of the resignation, surely its interests do not.

It publishes its findings to protect the public. And to assure that the public is fully protected, the boards and professional societies would seem to be obligated to investigate to see if the substandard practice before the SEC warrants further action on their part.

This is not to say that there can or should be complete uniformity in ethics enforcement or that a member who has been suspended from

the Institute or from a society for, say, two years should necessarily suffer a like suspension of his certificate.

Different values, different considerations, different responsibilities and different legal considerations of the various organizations come into play. But what I do mean to suggest most strongly is that when a person is disciplined by any disciplining body, that action is of concern to all other such interested bodies and they should investigate the underlying causes and take whatever action they deem appropriate. They just can't continue to ignore each other's work.

President Giffen expressed the feeling that one way to assure compliance was to exchange disciplinary information among the interested organizations on a formal routine basis. To that end, he pledged that the Institute would notify state societies and boards of any disciplinary action taken against their members and registrants and asked that the societies and boards do the same with respect to actions involving Institute members.

This pledge was predicated on the advice of Institute's legal counsel that there was a minimum danger of libel action being successfully prosecuted against the Institute as a result of its good faith disclosure of information regarding Trial Board decisions to parties having a legitimate interest in such actions.

The legal counsel of some state societies take a more restrictive view. Some say that specific bylaw authorization is necessary for even this limited exchange of information regarding decisions in disciplinary hearings. Others permit a full exchange of all information pertaining to the case so long as the bylaws specifically authorize it.

The factors influencing these restrictive opinions are easy to understand. Counsel's job is to keep his client out of legal difficulties. The more conservative the opinion, the less danger there is that the client might be sued.

However, we should concern ourselves with the broader challenge imposed on the profession as guardians of the public trust. Granted, we should avoid lawsuits, but in doing so, need we take the easiest or safest road? In view of our responsibilities to the public and the profession as a whole, rather than to ask legal counsel, "The Institute wants to know why we expelled one of their members from the Society. Can we tell them anything?" should not our question be, "How far can we go in exchanging information with other professional bodies having a legitimate interest before incurring a material risk of suit?"

The Illinois society action could be taken as a model. In response

to President Giffen's letter, the following bylaw was adopted:

> The officers, directors and employees of the society are authorized to obtain information from and to provide information to the officers, counsel and employees of the American Institute of Certified Public Accountants on matters of mutual interest, including information concerning members of the society and applicants for membership in the society. If information concerning a member or an applicant for membership is furnished by the society to the Institute, it will be provided only upon receipt of a written request for such information from the Institute.

I am quite sure that the Illinois society would feel flattered to have its language appropriated by any organization represented here today. It offers an effective and a practical way of doing what needs to be done.

Assuming steps are taken to meet any reservations of legal counsel concerning the exchange of information, at what stage should information be exchanged?

It usually takes the Institute from six months to a year for a complaint to be investigated by the ethics committee and subsequently be determined by the Trial Board. After such a determination is made, it seems quite clear that there is little risk in our notifying interested state societies and boards of the suspension or expulsion from the Institute of one of their members or registrants, and Bill Caldwell reported in his talk that this is basically the position taken by the Kentucky Attorney General. But since it takes so long for an erring member to be disciplined, consideration should be given to exploring whether information can reasonably be exchanged at an earlier stage. This would be desirable for several reasons.

The basic purpose of any disciplinary action is to protect the public by penalizing unscrupulous or substandard practitioners. To fulfill this trust, a hearing of the charges should be had at the earliest possible time so that if found guilty, the practitioner may be appropriately penalized. This principle applies equally to each of the professional organizations. In addition, every effort should be made to resolve the issues as soon as possible so that the respondent is not subject to the anxiety of the disciplinary process for a longer time than is necessary.

We should consider, therefore, whether we can move forward the point of time at which disciplinary information is exchanged. For example, would it be practical or desirable for the Institute to notify a society or board of the nature of a complaint concerning a member or registrant? If a member is alleged to have been convicted of a felony

and the ethics committee has court documents proving the conviction, it would seem reasonable to exchange the information as soon as it is received and this would, at all times, be while the matter was still under investigation and prior to the time that it is referred to the Trial Board.

If the complaint concerns substandard work, different considerations come into play. In the conviction cases, a determination of guilt has already been made by the courts. With complaints involving substandard practice, the initial determination of whether there are, in fact, any grounds for the charge must be made by the ethics committee itself, which is charged with investigating complaints.

A few months ago, we asked counsel for the Institute to consider whether it would be legally possible as a part of the committee's routine investigation, to notify a state board and society concerned that a complaint had been received, set out the substance of the complaint and ask whether the other bodies had any information which would be of assistance to the committee in its investigation. This procedure would seem to have several advantages.

First, all agencies concerned would be on notice of the complaint. Knowing that the Institute was considering it, they could either pursue it independently or await resolution of the case by the Institute. If the other agencies' investigations are further along than the Institute's, the Institute might prefer to await their findings. In any event, there would be cross-knowledge and, hopefully, co-ordination.

Second, the CPA complained of would know that the matter is before the board, the state society and the Institute, all at the same time, and could respond to all of them appropriately. Two questions arise: First, does such a practice present unreasonable risks of lawsuit and second, is such a practice desirable from a policy standpoint?

As to liability, Institute counsel has informed us that the trend of the law appears to provide greater protection to membership organizations in disseminating information about members. Cases involving members of labor unions have sustained the right of the union to publish information relating to members' fitness for membership and loyalty to union ideals. It is not entirely clear what claim to public trust unions have, but it would seem that professional organizations, because of their responsibilities to the public, are in an even better position than unions to disseminate to properly interested parties information concerning a member's or a licensee's fitness to be a CPA, or a member of the professional organization.

We feel that there is sufficient protection that from the legal point of view we can offer to exchange information on complaints to proper parties at the earliest point possible.

There is still the policy question whether this is desirable. We have found that some Institute members faced with charges before both the Institute and the state board have adopted different defenses for each of the two bodies.

They may, for example, wish to represent themselves at the trial by their professional societies or by the Institute on the theory that this is essentially a trial by their peers, while they would choose to be represented by legal counsel in the state board proceeding at which their right to practice as a CPA may be in jeopardy. In addition, they may make admissions to their professional organizations that they would not make to their licensing body.

The basic question is whether the Institute, for example, desires to pass on to other bodies a complaint against a member, the validity of which has not yet been assessed by the ethics committee. Suppose the complaint was passed on to a state society and the ethics committee later found that it was groundless? Would the transmission of the finding of "not guilty" be sufficient to wipe the slate clean, or would the member, nevertheless, be harmed in the eyes of his society by the mere notification of an allegation of misconduct?

I would argue strongly that a member is not discredited by being complained against and I am sure that most persons who have worked in the ethics field would agree than many complaints which come before ethics committees are groundless.

This question is therefore a matter of policy which will be considered in due course by the Institute's ethics committee and perhaps later by the Institute's executive committee. I submit, however, that it's a proposal worthy of your serious consideration in the panel sessions which will follow these talks and your reactions to it would be very helpful to us.

There are great advantages to be derived from intra-professional communications of this type. As an example, through the Institute's Washington office a few years ago, the ethics committee was alerted to testimony of a member before a Senate subcommittee. Since the testimony raised several ethical questions, a case was opened and the member was asked to comment on the points raised. His reply was satisfactory to the committee, which then wrote to him, thanked him for his co-operation and told him the case was closed because no violation had been found.

In the meantime, and without the committee's knowledge, the state board of accountancy was conducting an investigation concerning the matters about which the member testified to the Senate. The board's investigation was broader than the Institute's. The CPA defended before the board by showing the letter written on behalf of

the Institute's ethics committee indicating that no violation had been found on the facts considered. This was an obvious embarrassment to the board and to the Institute. After an extended board hearing, the member's certificate was revoked and the case is currently in the courts. We would hope that the courts will recognize that the Institute's action was based upon a more limited set of facts than the board's and does not constitute an approval of all the member's activities. The matter is again before the Institute's ethics committee, but no action is likely until the court action is resolved.

The story highlights the desirability of exchanging information at an early stage. It also points up some of the problems involved.

Suppose the board had had no complaint against the member and suppose further that the Institute learned of his Senate testimony, opened the case and notified the state board and society that he was under investigation or, as the Institute's bylaws put it, "under charges." Suppose the Institute's committee decided that no violation had been shown. Has it harmed the member's professional standing by disseminating information before making this determination? Should it notify the society and the board before closing the matter, or having notified them initially, should it notify them first of its intention to close the case? What if they object to its being closed?

Can any of the bodies really dispose of the matter without knowing what the other investigations have turned up and if all the bodies have the same information, is it not fair to conclude that the finding of guilt or innocence of the charge should really be the same among all three bodies, even if the penalty assessed by each with respect to such guilt is different because of their varying interests in the matter?

Clearly there are problems when a complaint is filed with one body and all of the bodies are to be notified of the charges. But the disciplinary effort would be greatly strengthened by such an exchange, to the obvious benefit of the profession as a whole.

There are fewer problems, of course, if notification is made after a preliminary determination has been made by the ethics committee and the case is set down for a trial. But, with such procedure, the time during which the CPA is exposed to the disciplinary process is necessarily extended. As I mentioned, there seems to be little problem in exchanging information after the disciplinary action is taken, except that widely disparate results might occur; and when I refer to information in any of this context, I mean at least a copy of the charge and the basic supporting documents underlying the charge.

We feel that even more than this can be legitimately exchanged—even the transcripts of hearings—but again, this is a subject for your discussion today.

All this points up some of the problems the profession faces in its

multiple jurisdictional structure. We now have the SEC, the state boards, the state societies and the Institute, each with its own disciplinary powers. Thought should be given to alleviating this duplication.

Presently, a member charged with unethical conduct may be faced with four major hearings and perhaps several minor ones before local committees. On analysis, however, a similarity in the interests and positions of state societies and the Institute appears in that they are both voluntary professional organizations. Consideration might be given to the possibility of combining these groups' disciplinary efforts.

For example, would it be desirable for the society and the Institute to hold one joint trial before an impartial board consisting of members of both the society and the Institute, with the ethics committee of each group collaborating on the presentation of the case and with the decision applicable to the status of membership in both the society and the Institute?

Or might it be desirable that the Institute turn over to the societies enforcement of the rules dealing with professional behavior—solicitation, advertising, encroachment and the like—while the states turn over to the Institute enforcement of the technical standards, with the decision of each body affecting the membership in the other? This seems a reasonable division with respect to our responsibility, since what constitutes professional behavior could probably be best handled on a local level while the Institute as the body which sets technical standards might better concern itself with violations of those technical standards. Of course, either of these possible solutions must be preceded by a greater uniformity of codes and trial procedures than now exist.

State boards are in a somewhat different position since they are hardly voluntary professional organizations and are probably more restricted by law in what they can do, but if for example state boards can make use of the uniform grading service for the CPA exam, might they not also be able to make use of the findings of a hearing board some of whose members are members of the state board, the others being representatives of the state society concerned and possibly of the Institute?

Perhaps the legal problems in this suggestion are insurmountable. Perhaps only state board members can sit on the hearing panel. If so, can the society be responsible for developing the case, then presenting it, as prosecution, to the board? Perhaps none of these suggestions will ever be adopted because the organizations concerned will not want to give up their sovereignty, will not want to let anyone else determine the fate of their members.

If this is the case, other avenues should be explored since the present situation is inefficient, expensive and sometimes unfair to the re-

spondent. This is another possible subject for discussion at your panel sessions.

The disciplinary effort is plagued by two major problems: the lack of funds and the timidity, if that's the word, to fully enforce ethical standards. The latter attitude often stems not from fear or disinterest, but from a natural concern over the welfare of others in whose place we could easily see ourselves.

The financial burdens on state boards in disciplining registrants are considerable. Travel and available time are involved. Legal counsel must be retained. A record of the proceeding must be kept for reference in the event of a legal challenge.

While this burden can be handled by many states, we know of several where the holding of one hearing drained the treasury for the year.

One answer may be to raise registration fees, many of which are extremely low, when one considers that what is involved is a license to earn a living as a CPA. Many professional society dues rates exceed the board's registration fee and if CPAs will pay the greater amount voluntarily to their professional society, why cannot the compulsory registration fee be at least in an equal amount?

If legislatures will not permit an increase in fees, perhaps the CPA society can apportion a percentage of its dues to support state board activities. One of the members here suggested to me yesterday that in his state, at least, this would be a legal impossibility since the Attorney General is of the opinion that a private organization cannot support a state body in this way.

I've discussed now two of my original three points: the exchange of information at the earliest stage and the possibility for improving the machinery for enforcement. My final point is whether there is sufficient awareness of professional ethics and concern for its enforcement among practitioners.

As to basic awareness, it seems that the accounting profession suffers from the same lack of exposure to ethical principles in the pre-entry years as other professions. I know of only two law schools which give a formal course on legal ethics and these are one credit exposure courses. I don't know of any college having a formal course in ethics for potential public accounting practitioners although many colleges, I understand, attempt to weave ethical considerations throughout their accounting courses.

Many state boards now give an open or closed book ethics exam as part of the CPA exam and several state boards give complimentary copies of *Ethical Standards of the Accounting Profession* to successful

CPA candidates. We recommend both of these activities to those of you who have not yet adopted them.

How many state societies or boards promote awareness of ethical standards by offering to present programs on professional ethics to collegiate accounting clubs? How many firms include in their training programs a course on professional ethics? Since ethics is largely a state of mind—a professional attitude—perhaps it can be learned best within the firm from the men who have developed it and lived it.

But even if every practitioner is fully aware of every nuance of professional ethics, the system is doomed to failure unless, when substandard work or unethical practice by another comes to a person's attention, he takes the appropriate steps to see that it doesn't happen again. These steps can take many forms.

If the matter is minor, the practitioner might want to contact the erring CPA himself or he might wish to report the matter informally to a member of the state board or the state society ethics committee, so that a phone call or a personal contact can be made by one of these men in his official capacity. Many minor, unintentional violations in the professional behavior category can be effectively handled in this way. But as Bill Caldwell previously mentioned, informal handling can be dangerous because it may fail to disclose a trend which the society or board should know about.

Minor violations of the technical standards which seem not to warrant disciplinary action are often referred by the Institute's ethics committee to the practice review committee, as an educational matter. Matters submitted to the practice review committee in the first place cannot be referred by practice review up to the ethics committee, no matter how serious the matter is.

In speaking to a few of the delegates, I've found that their procedures forbid the ethics committee from turning anything over to practice review. However, since the Institute's practice review committee provides educational services only and has no disciplinary function, we don't face this problem at the Institute.

The important thing is that improper practices not go unchecked. More serious matters or repeated minor infractions, of course, require formal handling before the professional societies and boards. The important thing is that they not go unreported.

We need a massive educational program to remind practitioners of their responsibility to bring complaints to the proper authority. Nobody likes a "squealer" and few of us want to be our brother's keeper, but as John Lawler noted in his Managing Director's Report to Council a few weeks ago, "squealer," "rat" and the like are the jargon

of the underworld and such expressions should have no place in the dictionary or lexicon of a profession. When a practitioner defends by saying, "Sure, it's wrong, but everybody does it!" his violation is far the worse for not reporting "everybody" in the first place, or at least trying to make them stop the undesirable practice.

Until we can say with confidence that when a practitioner learns of substandard work or unethical behavior by another, he takes appropriate action, we are not truly a self-disciplining profession. I submit to you that it's all one "ball of wax." All violations must be effectively dealt with and, as a first step, all violations must be reported. They won't be reported unless we can deal with them effectively and we can't deal with them effectively unless we find a way to better co-ordinate our efforts.

With co-ordinated efforts, the accounting profession can have a disciplinary record second to none.

Discussion

Mr. Richard Helstein: Might it not be a first step in establishing communications if you would send copies of Institute counsel's memorandum to the various state societies so they can submit this to their counsel for review?

Mr. Schneeman: We don't have this in a written opinion yet, Dick, but if we can get a written opinion out of him, we'd be willing to. I'm sure we can research the question and get the appropriate law.

Speaker from the floor: I would like to direct a question to Mr. Schneeman.

At what level, or what degree of seriousness would you like to have state boards report violations to the Institute?

Suppose you have a very minor infraction and you call the man in and discuss it with him and the matter is settled. Would you notify the Institute?

Mr. Schneeman: I should think if, on the local level, you're satisfied to handle a complaint in this informal way that we probably shouldn't be notified.

On the other hand, this is probably a question that the ethics committee could answer better than I could because I don't mean to set policy for them.

I think we should be interested in getting as much information as

possible on all practitioners, even if it's minor in nature, so that at least it can be noted in the files that we keep.

Probably the fact that the state board took an informal action and was satisfied with it would indicate to the ethics committee that they should do similarly.

It would, I think, help the state board's action for the Institute's ethics committee to write to the man also and say that this infraction has been called to their attention and that they concur with the state board's finding. This wouldn't require a hearing at all before the Institute, but it would show the practitioner that there is co-ordination between the different bodies and that he should behave in the future.

Third Session

Implementing Ethical Codes

A Mock Trial

Over the years, the Institute has often been asked by state societies and by some state boards of accountancy for information and assistance in conducting their first disciplinary hearing.

To examine the types of problems encountered in disciplinary hearings and to illustrate how a fair trial can be conducted, a mock trial was held during the third session of the conference. The charges were taken from previous matters brought before the Trial Board by the Institute's ethics committee.

The procedures followed were identical to those of an actual trial, except that the internal discussion of the Board members leading to their decision, which in an actual trial would be in closed session, was conducted at this hearing in the open.

The discussion following the trial showed again that men will differ in determining guilt and in imposing a penalty once guilt is established.

While the session seemed to be of more interest and perhaps greater value to representatives of states which had little experience in conducting hearings of this sort, it was felt that all benefited from the presentation.

Because it would be difficult to properly edit the transcript of the hearing to a size which could be accommodated in this booklet, only this factual statement of the session is included. However, state societies and boards of accountancy who are interested in reviewing the transcript and exhibits of the trial are invited to contact the Institute and the transcript will be made available to them on a loan basis.

Fourth Session

The Conference Concludes

Marvin L. Stone . . .

The basis of every profession is a body of specialized knowledge.

The professional skill that we have leads to power from which stems social responsibility, as does all power.

The use of our professional knowledge also requires judgment and the public is entitled to feel that our professional judgments are made with the public's best interest at heart and that we don't have any personal axe to grind.

A professional man can serve the public effectively only if he serves in an atmosphere of public confidence and public trust.

When our public has no confidence in us, we have little to offer society.

A profession must discipline itself to merit and foster this public trust and confidence. A layman, certainly, is not qualified to specify or enforce ethical rules. And, of course, rules are useful only if they're enforced. Consequently, enforcement is necessary if rules are to have meaning.

This ethics conference, the first of many, I hope, is living proof of CPAs' concern for this obligation to the public.

The enunciation of ethical rules, as all of you well know, is very, very difficult. It is a most serious problem and a most difficult one.

And the application of these rules, as you perhaps noted in the mock trial this morning, is even more difficult than their enunciation.

The observance of ethical rules is largely a matter of self-discipline. While the threat of penalties might deter a few, the preponderance of CPAs observe rules of professional conduct because of their own moral code and personal convictions.

If the preponderance of CPAs were unwilling to obey the rules, there's no way on earth that we could enforce their observance.

Similarly, if the general public were all to engage in stealing, it's

obvious that no police force, of whatever size, could keep citizens from stealing.

So it is then with any type of enforcement. Primarily, we must rely on the people's own moral code to promote enforcement.

In my opinion, the preponderance of ethical infractions are due not to willfulness, but to ignorance. This suggests, then, a need for greater educational efforts to dispel this ignorance.

I don't mean to suggest that we limit our present enforcement procedures, because I believe they are also important. A rule without enforcement is without teeth.

However, while we can enhance compliance through enforcement, I think the basic problem in professional ethics is one of dispelling ignorance of the standards. If our educational efforts were increased, we would find less and less need to impose disciplinary sanctions.

Now to put the discussion of ethics into perspective, I'd like to talk about one particular ethical rule, perhaps the most important one.

This rule is contained as part of Article II which deals with technical standards. It is Rule 2.02 which provides that a CPA is guilty of an act discreditable to the profession if he is materially negligent in the conduct of his examination or in making his report thereon.

Enforcement of this rule has always been hampered by the fact that it's very difficult to uncover information as to whether negligence has actually occurred. First of all, negligence can't always be uncovered by reading a report alone. Such a review might uncover negligence in reporting standards, but it certainly isn't going to uncover, in most cases, shortcomings in the working papers or in the actual audit procedures that only a review of working papers would disclose. Therefore, a work paper review is basic to any investigation of an alleged technical noncompliance.

Enforcement of this rule is also hampered by the unwillingness of third parties to disclose information which would lead to a review of the work papers or the audit report. In this lawsuit-happy world in which we live, bankers and others using financial statements are very hesitant to disclose information since they might be subjected to a liability suit brought by the CPA, the client or any third party who may have been damaged.

So our work in enforcing this rule is made very difficult and we must rely to a large extent on voluntary compliance.

Also, the nature of our profession's work makes a review very difficult.

All the work of physicians in hospitals is under constant review. There are tissue committees, and other types of committees, which look over the physician's shoulder and police his professional work.

Lawyers' courtroom practices are public and are under surveillance of other lawyers and the court itself. This, of course, is not true of all legal work, but at least to that extent a lawyer's work is under some degree of surveillance.

An architect's plans, in most areas, must meet building code requirements and many of the plans, at least for very large buildings, are actually scrutinized by engineers and architects in the employ of regulatory bodies to determine whether they meet required standards.

Our work, however, just isn't susceptible to review in the same way. We don't work in a hospital or any comparable place. There is really no place for the equivalent of a tissue committee. When we represent our client in adversary proceedings, they're normally done in private and not in public, and consequently they're not susceptible to the same degree of surveillance imposed upon a lawyer in a courtroom.

And, finally, our mistakes probably wouldn't show up so obviously in our reports as would, for example, an architect's omissions which might be found in a review of his plans. You normally need not build the building to discover that the architect's plans are unsound.

Possible defects in our reports are not self-evident. From a mere reading of an audit report, it's difficult if not impossible to determine whether the auditor really did all the things that he should have done before issuing that report.

Our profession has made many efforts on both the national and state level to eliminate substandard work.

In our state, and I'm sure in many others, volunteer practice review committees have been organized. In some states practitioners may turn in work papers for review. The purpose of such reviews is education, not discipline.

In Colorado, and I'm sure in other states, the state society reviews financial statements which have been made public, such as United Fund audits and audits of municipalities. The society then calls to the attention of erring CPAs those areas in which reporting standards seemed to be inadequate.

Obviously, this type of review is limited primarily to reporting standards. Only the most obvious inadequacies in field work are likely to be detected.

The submission of substandard reports by credit grantors for professional review has always been limited by their concern of legal liability.

In one city, a bank was sued by a CPA after it had, at the CPA society's request, turned in an audit report to see if it was substand-

ard. As a result the bank found itself the defendant in a lawsuit. This lawsuit has been cited to us by many credit grantors in other parts of the country when we try to encourage them to co-operate with us.

So we face a confidentiality problem whenever we attempt to ferret out substandard work. Other professions solve this problem in a way not readily available to us. For example, a patient entering a hospital is usually asked to sign a statement which permits the hospital to release information about his treatment. It would be hard to imagine a CPA's client signing a statement which would permit the CPA to disclose confidential information about the client to third parties.

The concept of confidentiality is probably the largest road-block to a comprehensive and constant effort by the profession to ferret out improper work.

Even the work papers themselves would be of limited use in many respects. If someone indicated in his work papers that he had performed certain required steps when he hadn't, there's really no way to uncover his dishonesty from the work papers alone.

There have been a number of serious proposals put forth by CPAs as to how we might police ourselves more effectively to upgrade standards and eliminate substandard work, but all of these suggestions tend to gloss over the confidentiality problem.

A professor in New Zealand, Edgar Stamp, has put forth a rather interesting proposal, which was really addressed not to substandard work, nor to ethical considerations, so much as it was to the upgrading of accounting principles and the improvement of uniformity.

He proposed an accounting court supported by assessments on CPAs. Paid CPAs would sit on the court as judges, and would decide whether the accounting principles reflected in the audited financial statements were proper. The judges would then issue, in effect, an opinion of their own.

The CPA who did the auditing would be obliged to cite any issues which he felt were cloudy and he would indicate his opinion as to which principle he felt should be used. The accounting court however would have the final say.

The idea has much merit, since it would bring into the open many of the decisions which are now made in closed rooms by all of us. It would produce a large body of precedent that accounting theorists would have an opportunity to examine. They could see some of the things we do and perhaps learn something from them, in the same way that law students learn from reported cases.

However, the time lag implicit in this proposal, and the numbers of CPAs that would be required to do the tremendous amount of work, make the idea impractical, in my opinion.

The use of compulsory inspection teams is another approach. Many of the large firms and CPA firm associations now have quality control programs whereby teams go from office to office and perform a post-audit review of work papers. Some smaller firms may also do this on a co-operative basis.

The program, of course, creates a confidentiality problem when review is carried out by non-firm members. A client's work papers certainly may not be shown to anyone outside your own firm without the client's permission. In addition, the sheer size of this task would be enormous if, for example, a periodic inspection by a team from the Institute or the state societies were compulsory.

Such a review could only be done by CPAs and the number of CPAs presently available is inadequate to keep up with the demands of regular work.

The Institute's planning committee has made an accreditation proposal which is similar but not compulsory. They recommended that accreditation be made available to any firm that wishes it by permitting an inspection team to come in. The firm would pay the cost of the inspection and would receive some type of stamp of approval if it passed muster.

All of these approaches are meritorious, but I think they all fail, for one reason or another, usually because of cost or cumbersomeness or the time lag involved.

Since most substandard work, in my opinion, is due to ignorance rather than willfulness, I suggest that we attempt to dispel this ignorance by requiring compulsory education.

Therefore, at the risk of being not only the youngest Institute President in thirty years, but also the one holding the office for the shortest period of time, I submit a suggestion of my own regarding a compulsory education requirement.

I recommend that each CPA be required to show periodic evidence of continuing education in order to maintain his right to continue to practice. Most states now require a CPA in practice to acquire an annual permit. I suggest that the annual permit be issued only to CPAs who submit evidence that they have spent a week of study during the year. This study wouldn't necessarily need to be at college. It could be at tax institutes, professional development courses or any type of technical meeting that would keep them current. I would not specify the type of education because, obviously, a tax specialist would require different courses than would a person in management advisory services or on the audit staff.

And I wouldn't necessarily require that the courses be taken every year. A requirement that three weeks' education be taken every three

years would permit a CPA to take a longer program every two or three years.

Now this may seem a little severe. However, I just can't see any other way of knowing that we are reaching those practitioners who, once licensed, never get back to any type of academic exposure; never go to a CPA society meeting; never open a newsletter; never open a book to further their professional knowledge.

I would suggest that this education be required by state boards rather than by the Institute or the state societies because, in my opinion, this is the only way the requirement has teeth. An Institute or state society compulsory education requirement would probably succeed only in diminishing the membership rolls.

Therefore, I suggest that we get right down to where the idea has teeth and that's at the state board level. I'd suggest the requirement be included in state board rules in such a way that a practitioner who failed to comply would lose his license to practice.

I would suggest no "grandfather" clause because I am less concerned about the new people than I am about the old.

Doctors in every state are required, by their hospital, to maintain a certain level of attendance at hospital educational meetings to remain on the staff. Since a doctor without hospital privileges is pretty well out of business, this requirement has more teeth than may seem to be the case.

The accreditation of hospitals provides additional teeth because the hospital association insists on adherence to certain educational requirements before it will accredit a hospital.

A group of doctors called the Academy of General Practice has gone even further. This 30,000-member organization that has been in existence about seven years requires its members to furnish evidence of at least 150 hours of education every three years in order to retain membership.

Since this is purely a membership organization, a member is not disenfranchised if he fails to comply. He does not lose his right to practice.

However, enough members have felt it necessary and advisable to remain a member of the Academy that they have continued during these seven years to do what is necessary to maintain their membership.

Of the 30,000, you might be interested to know, 10,000 have agreed to take a voluntary examination that's going to be given next July. This is the first time that the Academy has given such an examination. A member who fails the examination will not lose his membership in the Academy; however, he will no longer be a fellow member. A num-

ber of specialty boards in medicine apply this same technique. A member must pass an examination to be designated a fellow member.

The Academy of General Practice requires that 50 of the 150 hours be taken as a part of a course at a medical school or at one of the accredited courses given by the Academy. The other hours can be taken at any type of a workshop, institute or educational meeting, other than a pure business meeting of a hospital staff or other professional group.

Some CPAs will probably say that experience is the best teacher and that there's no need for a compulsory education requirement since we're getting a great deal of education every day we're in practice. I do not demean the importance or the value of experience. However, I don't think there is any substitute for academic refreshers.

Much of the experience to which many CPAs are exposed is shallow in nature. In too many cases "experience" means only continuous repetition of the same low level work.

A person practicing at this level often fails to keep up with current developments in accounting, auditing and all the related fields. He is simply not serving his client in the manner in which the client is entitled to be served.

An interesting book by Howard Ross called *The Elusive Art of Accounting,* a book that I can recommend to all of you, says that accounting is the language of business, which is a quote we've all seen many, many times. But then he points out that as a language it's really not a body of philosophical concepts, and consequently, it's continuing to evolve in the same way that language is. A thirty- or forty-year old dictionary would be pretty well out of date. And so is the information in the minds of many of our practitioners who haven't taken an academic refresher for thirty or forty years.

As I said before, CPAs are licensed to protect the public. I would think that real protection requires something more than a one-time evaluation or accreditation. Our license grants us a legal monopoly and a legal monopoly carries with it a responsibility to give the public everything to which it is entitled. The monopoly which we have been given can also be taken away if the public does not receive the service it deserves.

A compulsory education requirement, of course, is not the whole answer.

Ideally, perhaps we should all take an examination every three to five years. I reject this idea, because I think it goes too far to be practical.

Since we all travel such diverse routes, it would take a multitude of examinations, not a single examination, to test us adequately.

Upon entering the profession, CPAs share a common core of knowledge, but by the time each CPA has been in practice five or ten years, he is traveling a road different from that of many of his colleagues. Some travel the tax road; others are in operations research; others are in auditing; and others are in systems work. Many different examinations would be needed to test CPAs who practice in such divergent ways.

Consequently, I don't think the examination route is practical and I really don't think it's necessary. I believe, as I've said before, that most of the ethical infractions are the result of ignorance. If we get to the heart of the problem with compulsory education, I believe we can dispel much of the ignorance.

Whether or not my proposal is adopted, all the present efforts to ferret out substandard work should continue—the practice review committees, the review of public files, the awareness of the obligation for self-discipline.

I don't believe that any of this is wasted effort by any means and I think it should continue. The nature of our professional work makes self-discipline essential. Society, however, is bound to protect itself. If we don't discipline ourselves, the government will.

The loss that would follow from such an occurrence would fall not just on the regulated professional alone, but even more heavily on society generally. For when the government feels it is necessary to regulate a business or a profession, it usually does so by the means of some special agency.

Such a regulatory agency is likely to be given not only law-making functions, but judicial and executive functions as well, short-circuiting the proven principles of checks and balances, and of due process.

Happily, both the machinery and the spirit of self-discipline are strong in accounting, as your presence here attests. But the task is never-ending and that is why the examination of professional ethics, which you have been undertaking here is so important.

Keith A. Cunningham . . .

Two impressions came out of the morning panel sessions: First, the profession faces formidable tasks and, second, there is no paucity of good ideas on how to cope with our problems. I think we have a good deal to work on in future meetings.

My function is that of a reporter, but naturally I have to be an editor too, because I had to select from the discussion groups those things I thought to be significant; my emphasis may be somewhat different from yours. Therefore, if my reporting is faulty, don't be afraid to raise questions at the appropriate time.

It seems there was a substantial overlap between the ideas discussion generated in the morning and afternoon sessions. As the day went on, some of the ideas that were generated in the morning were developed more fully. Accordingly, I'm going to try to limit myself to significant problems that were raised in the morning and leave some of the proposed solutions that matured in the afternoon to Wally Olson.

The speakers in the morning tended to set the scene for the discussion groups, and were rather specific in the area that each treated. The discussion groups, on the other hand, tended to develop rather broad problem areas and ideas about them.

The new form of practice before the Internal Revenue Service did not seem to generate much concern within the groups. There was a consensus that up to this time the new procedure has worked pretty well.

In addition, there was a consensus that the problem of disciplining is the profession's problem and should not be the problem of the Internal Revenue Service. Therefore, the conclusion was that the present procedure is preferable to the former procedure. However,

there seemed to be some problem in getting information from the Internal Revenue Service to process ethics cases. Some specific examples of this were discussed.

The second major item was an overall evaluation of the effectiveness of what the profession is doing today and the problems that we are encountering. There was a general feeling that what we are doing is good and that we have a right to be proud of our accomplishment.

On the other hand, there was no question in any of the participants' minds that there are some rather serious deficiencies. I think that we'd best discuss these deficiencies now.

There seem to be three areas in which enforcement problems arise:

The first of these might be termed activity reflecting upon the character of the individual and his fitness to practice in the profession. This relates to criminal prosecutions and to activity that raises a question of moral character. It was felt that in this area we are doing a pretty good job because it's the type of thing that we can get our teeth into. We have a court record, a judgment or a conviction that we can deal with. We don't have the problem of trying to ascertain the facts independently.

The second area dealt with relations affecting other practitioners. These are the relatively local issues, such as advertising, solicitation, and other things of that sort. There was a general feeling that we're doing a pretty good job in dealing with this particular area. There were some thoughts expressed that maybe there is a lack of definition of the standards in some of these areas.

Perhaps our present concepts about advertising, publicity, and so forth, still need development or challenge. Maybe we need more definite guidelines for practitioners in this area. However, the general feeling was that we're doing a good job of policing this kind of thing.

The third area—and this is the most important one—deals with activity or conduct affecting relations with third parties. This encompasses the problem of substandard practice, be it technical or otherwise, and here the majority of the groups felt that we are not really doing a good job.

We ask ourselves, then, Why aren't we doing a good job? What are the problems that we face?

First, as Marvin Stone indicated, there seems to be sheer ignorance on the part of those who are the violators in this area. There's a significant need for education, both of a technical nature and of an ethical nature.

Then, we have the problem of nonmembers of the Institute or state

society who do not receive the literature, and who in most cases don't participate in the professional development programs and other educational activities that are sponsored for the profession. This is a major problem area; to my knowledge, no real solution was developed in the discussion groups.

It was generally conceded that we have to do more educating, but the best way to implement an educational program isn't clear at this moment.

A second problem in this area is our inability to obtain the facts in order to deal with this kind of case. Now, why can't we get the facts?

There is a reluctance on the part of individuals to bring facts to the attention of the proper groups, whether they be ethics committees or state boards. This is a manifestation of a present-day social problem. We're dealing here with the same kind of reluctance to avoid involvement that we've seen when witnesses see persons being molested on the street and refuse to get involved. I think there's a social reaction developing today—a philosophy of noninvolvement.

A part of this reluctance of people to become involved appears to be cynicism on the part of a significant group within the profession who feel, "Well, we're not going to get the right results in any event. We're only going to hurt ourselves one way or the other if we pursue this complaint." We've all heard the complaint that one party gets a different kind of treatment than another. Justified or not, an unfortunate tension exists between the big and the small firms.

Another problem arises in our dealing with widely publicized cases involving pending litigation; counsel for a respondent called to task for violating our standards has often charged, "Look at all the cases across the country; what have you done about some of these people?" You try to explain that your inaction stems from care not to impair a member's legal rights while litigation is pending, but some people just won't be convinced.

Just how to handle these cases is a serious problem, because some of them go on for years; our present tendency is to hold these cases in abeyance until there is some resolution of the litigation.

A corollary problem arises when you have a conviction in court and an appeal is taken. It takes time, sometimes years, to process the appeal. A critic may see only that this individual has been convicted and is still a member of the state society or of the American Institute.

We also have the problem of the multiplicity of jurisdiction that has been referred to on several occasions. As we've seen, an indi-

vidual may actually be tried for the same offense in five different forums.

A CPA may violate the rules of a federal agency and, in effect, be tried by them. The same offense may become the subject of a prosecution in a federal or state court. He may then be tried by the American Institute, a state society and a state board.

This presents a very serious problem, because there's something, we believe, fundamentally wrong with such a system that isn't compatible with our concept of American jurisprudence. So this is a broad area that we have to deal with.

We also have the problem, which is somewhat related, of communication between the many forums that have jurisdiction in these cases.

Here we find there are all sorts of restraints, some legal, some emotional and some political, that get wrapped up in the problem of communicating information from one agency level to another.

We have the problem of lack of uniformity between these various organizations. Our rules of conduct vary and in some cases, they vary significantly. It is possible for a member to be expelled from one organization while there is no basis for expulsion in another organization. There's a glaring inconsistency, in the public eye, when a member is expelled from one professional organization and yet remains a member in good standing of another.

We have the whole problem of the inadequacy of money and manpower at the state board level in many states. Now, this isn't true in every state, but it is true in many, many states. When we talk about resources, it must be kept in mind that we don't always talk only about money. We're talking about know-how. We're talking about staff. We're talking about the sheer ability and inclination to deal with the problems that we've identified.

We have the problem of the lack of public understanding. We've talked about the public's lack of understanding of the meaning of the reports that we render. Together with that is the total lack of understanding by some people of just what kind of results they should expect from the professional accountant. Of course, along with that, there is the problem of getting meaningful communication from people of this sort.

I referred before to the legal problems in the disclosure of information; this seems to become more serious all the time.

In fact, there was an article in *The Wall Street Journal* today about one of the medical grievance committees that had been sued by an ophthalmologist. He charged that their activity had resulted in an impairment of his practice, since he has lost referrals and other work

as a result of some publicity that had attended the disciplinary proceedings.

I'm sure that this is not a complete listing of all the problems that have been discussed in the morning panels, but these are the ones that seemed to me to be the most significant.

There seemed to be a general consensus that the solution to some of these problems was that in the long run, state boards are really the agency with which enforcement should rest. However, I don't think that anybody feels that it's feasible at this time to go completely in this direction.

So far as the legal problem is concerned, the thinking was that the Institute ought to offer more assistance to the state societies and even the state boards. We should attempt to arrive at a better definition of our legal position, and to give the local groups some assistance in dealing with these problems on a day-to-day basis. In other words, How do you correspond about these cases without exposing yourself to legal risk of liability?

Another problem area seems to be the inability in so many instances to fit the penalty to the crime. For example, all the voluntary professional organizations can do is expel the individual. We can't seriously impair his ability to practice. One of the factual situations cited here was a California case in which the individual was using a neon sign. Rather than take down his sign, he allowed himself to be expelled from the California Society. Since the state Board does not prohibit advertising, he's still a CPA. The story showed that this CPA apparently measured his membership in the Society against the value of the sign and decided the sign was more valuable to him.

It's pretty obvious that if we are to get at the really fundamental causes of some of these things, we ought to be able to prescribe education in some of these violations, particularly violations of the technical standards. I understand that this is being tried, at least in one or two areas.

It was suggested that, in cases of solicitation, we ought to be able to force the practitioner to withdraw from the engagement that he secured in that manner. However, problems have arisen with respect to even that kind of penalty, since if a client is satisfied and wants to retain the practitioner, we're in a poor position to say he can't.

Another area where significant problems exist is in the area of fees and their relationship to the quality of the work that's being performed. I think we've all experienced the circumstances in which it was pretty obvious that the fee was not commensurate with the scope of the engagement and the work suffered accordingly.

I was instructed to point out in this area that "the competitive bidding rule isn't dead!" That has a lot of ramifications that we don't have time to discuss here. But in this particular area, the fee area, I would like to suggest that Opinion No. 18 of the Institute's ethics committee has a lot of potential that we haven't completely explored yet.

Also, many of our fee problems stem from what I would like to call "the case of the apologetic practitioner!" I have seen many, many fee problems that arise when a practitioner goes to his client, with hat in hand, apologizing for the size of his fee before he ever sends a bill.

I understand that Louisiana has a very interesting rule on fees of successor accountants which I don't wholly understand, but which I think ought to receive some publicity.

Another area that was discussed was independence. With respect to fees, I think it was generally conceded that independence is fundamentally integrity, but that there might be a problem when a single audit fee is large in relation to a practitioner's total practice. Does this really have any influence upon his independence?

I think that covers the problem areas we discussed; I hope we can now work out the solution.

W. E. Olson . . .

One of the first problems we talked about in the afternoon discussion was whether or not we have really done enough to push the activities of our practice review committees; whether they were in fact effective; and whether or not they were desirable vehicles for education of our members at least in the area of reporting standards.

There were quite a number of mixed conclusions that came out of the discussions. I'll try to summarize these for you.

First, there was a general consensus that the effectiveness of practice review throughout the various states was mixed. Of course, in some states there are no practice review committees and some states are just now setting them up. It also became quite clear that many of the members, at least in one of the discussion groups, were not too familiar with what was being done by the American Institute's practice review committee. Few participants were aware of the fact that a publication had come out giving some statistics and information relating to the Institute's practice review experience.

I think this clearly indicates that we have a real education process on our hands even among ourselves—and we are supposed to be knowledgeable—on what is being done by these review committees. This group and the general membership must give them our co-operation and participation.

Some of the groups felt, however, that it was too soon to try to judge the effectiveness of these committees. They felt it would be unfair to conclude that practice review committees were not doing the job since they had been established so recently. The membership may not have had sufficient time to become thoroughly familiar with their activities and the ways in which they might co-operate with the committees.

I don't think anybody took the position that they were not de-

sirable. All the groups pretty much concluded that practice review committees were extremely valuable; that we ought to expend more energy in strengthening their activities and perhaps in making them more aggressive, particularly on the state level. One member of the Institute's practice review committee indicated that they had a very steady flow of work through their committee, which indicates that more and more reports are being referred to them for review.

I think we've heard mentioned several times over the last two days in various discussions, and in the discussion groups as well, that banks and credit grantors probably are not a good source for complaints of substandard reporting. Because of the legal liability problem, it's unlikely that we'll ever be too successful in convincing these people to refer many reports for review.

The groups concluded that there are two areas on which we ought to concentrate.

One is in our membership itself, which has to be the prime source for referrals of reports to the practice review committee. This indicates that we ought to concentrate on advising the members of the work these committees do and of what is expected of members in referring substandard reports to their attention.

The second source that everybody seemed to agree was a good one is governmental agencies. It was felt that in some states a good job has been done in co-ordinating the work of the practice review committees with governmental agencies with which reports must be filed. Where these are being referred for review, a good deal of work is being done in educating practitioners regarding compliance with the reporting requirements of these agencies.

One other conclusion that came out of the groups was that they would like to see the Institute be more active in sifting the complaints that come to the practice review committee from the federal agencies. It was felt that these ought to be sent down to the state practice review committees for handling. We didn't go into whether legal problems might exist in such a program.

As has been pointed out previously by President Stone and others, the practice review committees are probably limited in the range of education they can engage in, since most of what comes to their attention relates almost entirely to reporting standards. And most of them are purely educational and have no enforcement authority.

What's done in the field in relation to auditing standards usually does not come to the attention of the practice review committees, so we have to recognize that the area in which these committees can function is rather limited.

I'm sure I haven't covered all of the discussions, but what I have

reported is the general consensus about the work of the practice review committees.

The second major problem area that was discussed at length was the problem of the state boards not having adequate funds to carry on investigation activities in handling their cases. The questions were raised whether or not it would be practicable or desirable to have state societies attempt to provide needed financial support to the state boards, and whether or not it would be feasible to increase registration fees in the various states to provide the state boards with the funds needed to do a better job on the handling of their cases.

The general conclusion was that it would probably be impractical to try to get the states to adjust their registration fees to an adequate level to handle the investigation activity. In some states, the registration fees go into a general fund and would appear to be unavailable for the hiring of permanent investigators.

Some of the groups explored other possibilities for the state societies to help out in this investigation activity and it was felt that it not only wouldn't be proper for the state societies to try to provide funds directly to the state boards but in some states might even be against the law. It was felt that the state societies could do something else—that they might take on the investigation activity themselves, and finance this out of their operating funds. After completing the investigation, they could turn the results over to the state board for adjudication.

This would coincide with what Keith Cunningham mentioned earlier: that the key to the enforcement problem lies in getting the state boards to be more active and more aggressive in their enforcement activities.

In one of the groups, a question arose regarding possible conflict of interest if the suggestion was followed that the state societies carry on investigation activities and refer the information to state boards. It was felt that this wouldn't create any serious problem because the state boards would be free to accept or reject information, and to use it as they saw fit; they would not be restricted only to that information in any case.

There was also the feeling that there was a real need for close communication. This was a common thread that ran throughout all the discussions—the need for better communications, particularly with the state boards.

The third main area that was discussed was the proposition that there ought to be some consideration given to combining the Institute's Trial Board with the states' trial boards to eliminate what appears to be an unnecessary duplication. Earlier, Keith Cunningham

referred to the fact that in some cases a member could conceivably be subjected to hearings or trials at three different levels—governmental agencies, his state board of accountancy and his professional societies.

Certainly, there is an overlapping between the state and the Institute levels, but on this particular question, there were very mixed opinions. Many participants felt that the present machinery was desirable and should be continued, but that it probably needed a good deal of improvement. Communications between the three levels should be increased, and it should be clear which level should hear the complaint first.

Other participants felt that the matter ought to be studied in depth to see if the duplication between the state and the Institute could be eliminated.

One group suggested that perhaps the state societies ought to take over all of the enforcement activities and leave the ethics committee of the Institute to act or function as a high level policy group which would be persuasive in nature. To do this would require a change in the bylaws of the Institute which would provide that anything concluded at the state level would be binding on the members of the Institute.

There is, no doubt, some reluctance to do this until there is a greater uniformity of codes of ethics among the states and until the machinery in all the states is more adequate and more uniform than it is now.

Another proposal that was discussed was that behavioral matters be left solely to the states and that matters involving standards be left solely to the Institute. This is something that John Lawler has suggested in a speech before counsel. There was some feeling among the discussion groups that this proposal would not work; that the states would be reluctant to give up any part of their present responsibilities, and that they should be as much involved in standards as they are in behavioral matters, because at the local level they are more apt to get information concerning violations of standards.

In any event, out of these mixed views there was general agreement that the matter was worth studying and some further effort should be made to see whether there is a way of revising the present machinery to eliminate the multi-level problem. There was also the feeling that if the present machinery does continue in its present form, two things ought to be done.

It was suggested that a standard approach to communication between the Institute and the state societies and state boards should be developed. There are some beginnings in this direction, as mentioned

by Don Schneeman yesterday when he quoted the Illinois provision for exchange of information with the Institute.

A second suggestion was that some attempt be made to establish a priority for action on cases as they arise. It was felt that a case should first be reviewed at the state board level, that the second level should be the state society and the Institute should be the last one to deal with a case. It was hoped that a greater uniformity of conclusions would result.

In summary, the general feeling expressed was that three major areas needed improvement: (1) education of members; (2) better communication between the three enforcement levels; and (3) better co-ordination between those three levels.

Education, communication and co-ordination are the key words that were repeated many, many times in the discussions.

There were several individual recommendations in the education area: that examinations on ethics ought to be required of all CPA candidates and more emphasis placed on ethical matters in the CPA exam; that more attention ought to be given to ethics on programs of meetings of the state societies and the Institute; that members should be educated through more articles on ethics.

Regarding communications, there was a strong desire that there be a fast response among the three levels to requests for disciplinary information. And, as mentioned earlier, we need to develop a standard format or procedure to facilitate this exchange of information.

Finally, in reference to co-ordination, it was agreed that the primary need was to establish priority, and to arrive at some agreement between the three levels as to who would handle a case first.

Appendix

Opinion of Covington & Burling, Legal Counsel for the Institute, on Exchange of Disciplinary Information

Participation of American Institute of Certified Public Accountants in Exchange of Information Involving Disciplinary Matters Between the Institute, State Societies, State Boards and Other Authorities

February 29, 1968

The Institute has requested our advice on the degree of risk of liability for defamation (libel or slander) which might accompany the implementation of a program for the co-operative exchange of disciplinary information concerning member certified public accountants among the Institute, state societies, state boards and other agencies which have disciplinary responsibilities in respect of such accountants and which have filed with the Institute general requests for information of such character.

We conclude that the Institute may participate in an exchange of disciplinary information without material risk of liability, so long as it continues to observe the restraints that common sense and ordinary discretion would counsel. Under all but the most unusual circumstances, the current practice of preliminary verifying information of a disciplinary character whenever practicable before passing it on to other interested organizations should suffice.

Although we cannot guarantee that the proposed program for exchange of disciplinary information will not some day result in an action for defamation brought by an accountant so implicated, we do advise that the risk of successful prosecution of such a suit is so remote as to be immaterial in contrast to the benefit the proposed

exchange would confer upon the organized profession and the public.

The practice of individual certified public accountants may vary in scope and geographic range; disciplinary authority affecting their right to practice is spread among such agencies as the Securities and Exchange Commission, the Internal Revenue Service, and the various state boards of accountancy. While not empowered to take away the right to practice, the state societies and the Institute enforce among their members codes of ethics designed to maintain high standards of professional integrity and technical competence.

It is only logical and expedient that such organizations, governmental and private, charged with the enforcement of ethical and technical standards by law or by the general acceptance of the accounting profession, should co-operate not only in the formulation of standards but in their enforcement as well. The policing of the profession is as much a common duty as a common interest.

We contemplate that, when there comes to the attention of the Institute, by formal complaint, news dispatch, or otherwise, information indicating misconduct on the part of a member of the Institute, such information will be forwarded to those organizations reasonably thought, through his membership or license to practice, to possess a disciplinary responsibility in the matter without awaiting the completion of the Institute's own disciplinary process. By this procedure two desirable results are to be achieved. First, organizations other than the Institute will be alerted to the possibility of offenses within their jurisdiction. Second, by the adoption of similar disclosure programs or in response to the Institute's initial disclosure, it is to be expected that other organizations will supply the Institute with information helpful in the conduct of its own disciplinary proceedings.

The Institute would continue procedures reasonably designed to minimize the dissemination of false information adverse to the professional reputation of an accountant, but designed also to achieve reasonable efficiency and dispatch in promoting disciplinary enforcement. Thus, where relevant information comes to the attention of the Institute bearing its own evidence of reliability, for example, a release of the Securities and Exchange Commission or a statement purporting to have been verified from a source reasonably believed to be reliable, the information, together with disclosure of its source, would normally be promptly forwarded to the state societies and boards which reasonably appear to be concerned. It would be accompanied with a request that the recipient supply the Institute with any information at its disposal touching upon the reported accountant. On the other hand, when charges or reports lacking such evidence of reliability reach the Institute, the normal procedure would be to attempt

some reasonable preliminary verification prior to dissemination. This might be accomplished by a confidential letter addressed to and requesting the comment of the accountant concerned, whose unsatisfactory response or failure even to reply could be sufficient verification. If appropriate, the Institute might obtain certified copies of an Indictment, Information or Judgment of Conviction said to have been rendered against an accountant. A member of the Institute who lives or practices in the vicinity of the reported accountant could be commissioned to conduct a confidential and informal investigation.

In all cases, the Institute's disclosure and request for information would indicate at least the nature of the source of the Institute's information and an appropriate statement indicating the absence of verification by the Institute or the limited nature of the verification which has been undertaken. Any exculpatory information would be included, or forwarded subsequently if later discovered. In all but the most exceptional cases, disclosure to the appropriate recipients would precede hearing or disposition by the Trial Board or a subboard. There would also, of course, be disclosure of any final action taken by the Institute in the case.

As the circumstances that may be expected to arise will differ widely, we treat them here in a general way. Where there is doubt as to the fairness of forwarding a report on a member accountant, whether because of its nature or because the legitimate interest of the recipient is reasonably uncertain, it would be advisable for those making the decisions as to such exchange of information to obtain the advice of counsel, particularly at the outset of the implementation of such a program of exchange of information, when those making the decisions may lack experience concerning the factors which should be considered. In general, however, the touchstone for guidance is reasonableness and common sense under the circumstances.

To assist in understanding our position, we turn now to a brief discussion of the law of defamation, with more particular reference to what is known as the defense of conditional or qualified privilege. It is through this principle that the law recognizes the need of persons and organizations to communicate with one another on matters of common concern, provided that they do so reasonably, in good faith, and without improper purpose or motive.

Preliminarily, we must emphasize that defamation is a matter of state law. Responsibility for a particular communication will thus turn upon the law of the state in which it is published.[1] Though there

[1] E.g., *Diplomat Elec., Inc.* v. *Westinghouse Elec. Supply Co.*, 378 F.2d 377 (5th Cir. 1967).

is sufficient uniformity among the states for the law to be here set out in general terms, any state society or board planning to participate in the proposed exchange of information should request its legal counsel to determine whether local law would require that organization to follow a more cautious or limited approach than is contemplated here.

Essential to the understanding of a defamation action is that it is designed to provide compensation for injury to reputation, rather than injury to sensibilities.[2] The offense thus involves a communication to some person other than the person defamed.[3] The law offers its protection by recognizing as a legally protected interest one's right to protect the esteem in which others hold him.

Defamatory statements are made routinely, however, without the maker incurring material risk of liability. This evidences the fact that the law will accord to other legal interests—some in appropriate circumstances and some absolutely—a higher priority than the protection of reputation. For example, it is an absolute defense to an action for defamation for the declarant to prove the truth of his statement.[4] Dissemination of the truth, regardless of the speaker's status or motive, is protected at the expense of the victim's reputation. If the statement, unknown to the maker, is false, however, the defense of truth is unavailable and the maker must rely upon other defenses.

Nevertheless, there are many occasions on which defamations, subsequently proved false, are uttered without liability. They are, it is said, privileged. Absolute privilege shields certain governmental officers who speak in the course of their duties, even should they knowingly speak falsehoods or speak maliciously.[5] The interest in permitting them to discharge their duties without fear of responsibility for defamation is thought to outweigh the protection offered reputation.

It is a similar, but qualified, privilege that is available to protect the Institute, its members, and staff, as well as state societies, should a defamation action arise from the proposed exchange of disciplinary

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[2] 3 *Restatement of Torts* Sec. 559 (1938) [hereinafter cited as *Restatement*].

[3] *Restatement* Sec. 577; Prosser, *Law of Torts* Sec. 108 (3d ed. 1964).

[4] E.g., *McCuddin* v. *Dickinson*, 230 Iowa 1141, 300 N.W. 308 (1941); *Alexandria Gazette Corp.* v. *West*, 198 Va. 154, 93 S.E.2d 274 (1956); *Restatement* Sec. 582.

[5] Absolute privilege may also cover communications required by law or between husband and wife. See Prosser, *Law of Torts* Sec. 109 (3d ed. 1964). For cases involving governmental figures, see, e.g., *Scott* v. *Statesville Plywood & Veneer Co.*, 240 N.C. 73, 81 S.E.2d 146 (1954); *Elder* v. *Holland*, 208 Va. 15, 155 S.E.2d 369 (1967).

information.[6] This qualified privilege to defame is found in a great variety of situations. It has been summarized in these words:

> The proliferation of situations in which these privileges are allowed evidences a recognition that to conduct their day-to-day affairs, persons must communicate with one another concerning the people with whom they associate. In effect, the courts require only that a defendant act in good faith and as a reasonable man under all the circumstances, taking into account the importance of the interest which his communication will serve, the risk of harm to the plaintiff, and his own relationship to the interest and person involved. *Developments in the Law—Defamation,* 69 Harv. L. Rev. 875, 925 (1956).

Commentators have categorized the many situations giving rise to such a privilege by defining the interest served—that is, the interest prevailing over the protection of reputation—in terms of the parties to the communication. One formulation[7] lists five such overlapping interests supporting, if "sufficiently important," a conditional privilege if the maker knows or reasonably believes his communication will serve such an interest: (1) an interest of the publisher; (2) an interest of the recipient; (3) an interest common to the publisher and recipient; (4) an interest of some third person; or (5) a public interest.

It is obvious that whether the maker can reasonably entertain the belief that his statement furthers such an interest will vary according to the nature of the interest. Thus, if his own interest is involved, such a belief might be better founded than if it were solely the interest of the recipient or a third person. A may be privileged to tell B, a policeman, that he believes C intends to steal his car. In so doing he furthers his own sufficiently important interest in retaining his property by a communication designed to serve that end. A public interest in law enforcement would be served as well. Also, if B, as a prospective employer of C, asks A his opinion of C, then a qualified privilege attaches to A's reply, so long as it is uttered in good faith. A then would speak in service of B's substantial interest,

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[6] Regarding both privileges, it has been recently stated:

> Both as to absolute privilege and as to qualified privilege, the protection from liability to suit attaches by reason of the setting in which the defamatory statement is spoken or published. The privilege belongs to the occasion. It does not follow the speaker or publisher into other surroundings and circumstances.... *R. H. Bouligny, Inc.* v. *United Steelworkers of America,* 270 N.C. 160, 154 S.E.2d 344, 354 (1967).

[7] *Restatement* Sec. 594-98.

which B's request gives him reason to believe he furthers.[8] By the privilege, the law encourages a socially useful response.

In regard to the proposed program for the exchange of disciplinary information, the common, as well as individual, interests[9] of the Institute, the state societies, state boards and governmental agencies to which we have adverted should amply support the defense of privilege. Moreover, where disclosure of illegal conduct is made to a responsible governmental authority charged with enforcing the law violated, that occasion, too, is privileged.[10] There should be no need, as is sometimes the case when the communication would further no apparent interest, to offer disciplinary information only in response to a specific and detailed request. The necessity of such a request disappears where, as here, the interests served are sufficiently important and adequately identified. This would be so in the case of disclosure to a state society, if to the Institute's knowledge the accountant concerned can reasonably be thought a probable member of that society and that such society has a disciplinary interest in the alleged misconduct. Similarly, the interest of a governmental agency would be adequately identified were the accountant concerned reasonably thought to practice before it or to have been licensed by it and the alleged misconduct should be conduct in which such agency has a disciplinary interest. Accordingly, it should be necessary only that the Institute so conduct its program that, on a particular occasion,

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[8] See Prosser, *Law of Torts* Sec. 110 (3d ed. 1964). Were absolute assurance of a privilege here sought, our most conservative advice would be to make disclosure only pursuant to the recipient's request for disciplinary information. As one authority has put it,

> The defamer is privileged to respond to almost any request that is apparently made in good faith if the matter pertains in any way to the legitimate concern of the person asking information. 1 Harper & James, *Law of Torts* Sec. 5.25 (1956).

[9] The privilege has been described in these words:

> It is the general rule in the United States that a qualified privilege is recognized in cases where the publisher and recipient of the publication have a common interest which might be reasonably believed to be protected or furthered by the publication and the publication is made reasonably and in good faith.... *Kemart Corp.* v. *Printing Arts Research Lab., Inc.*, 269 F.2d 375, 391 (9th Cir. 1959), *cert. denied*, 361 U.S. 893 (1959).

It has been applied, for example, to protect a union official who libeled a plaintiff in a widely circulated union publication. *Sheehan* v. *Tobin*, 326 Mass. 185, 93 N.E.2d 524 (1950).

[10] E.g., *Foltz* v. *Moore McCormack Lines*, 189 F.2d 537 (2d Cir. 1951). The privilege may, on occasion, be absolute. See *Becker* v. *Philco Corp.*, 372 F.2d 771 (4th Cir. 1967), *cert. denied*, _____ U.S. _____ (1967).

the accountant reported upon cannot claim the privilege was abused.

Abuse turns upon the existence of actual malice, which we may presently define as improper motive or the lack of good faith. The shield of privilege could be lost if the plaintiff-accountant, with the advantage of hindsight, were able to establish improper motive or bad faith in the circumstances of the disclosure defaming him.[11] As we have said, truth, if proved, would provide an absolute defense. Were the report untrue, however, the defense would turn upon the presence or absence of privilege. It would be fatal to such a defense if it could be shown the maker of the report had knowledge of its falsity.[12] Some courts would require that the declarant have "probable cause" to believe his utterance true.[13] Knowledge of falsity, or absence of some reason to believe truth, establishes the malice necessary to defeat the privilege. The Institute would be well advised to indicate in its disclosure the nature of the source of the information conveyed.[14]

Similarly, malice defeating the privilege could be predicated on a showing of unreasonable dissemination. It would be unreasonable to furnish disciplinary information concerning an accountant to some person or organization not reasonably thought capable of acting upon it.[15] Thus, if the Institute were to receive word of the possible malpractice of an Iowa accountant, it would be unreasonable to forward it to the California society without some basis for belief that that organization could act upon such information in a way beneficial to the maintenance of high standards of ethics in the profession, either by disciplinary proceedings because the accountant was in fact

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[11] E.g., *Richardson* v. *Gunby*, 88 Kan. 47, 127 Pac. 533 (1912); *Annot.*, 26 A.L.R. 830, 856 (1923). One commentator puts it this way:

> A more comprehensive formulation might be that the defendant has abused a privilege when he does not act for the purpose of furthering the interest which the privilege is granted to protect. However, in most cases in which the courts use the term, they are not directly examining the motive of the defendant but are mechanically inferring the existence of 'actual malice' from his unreasonable conduct in making a statement. *Developments in the Law—Defamation*, 69 Harv. L. Rev. 875, 930 (1956).

It has been said of "actual malice" that "all definitions in substance come down to the equivalent of 'bad faith.'" *H. E. Crawford Co.* v. *Dun & Bradstreet, Inc.*, 241 F.2d 387 (4th Cir. 1957).

[12] E.g., *Caldwell* v. *Personal Finance Co.*, 46 So.2d 726 (Fla. 1950).

[13] E.g., *Baskett* v. *Crossfield*, 190 Ky. 751, 228 S.W. 673 (1920).

[14] See *Developments in the Law—Defamation*, 69 Harv. L. Rev. 875, 930 (1956), citing Prosser, *Law of Torts* Sec. 95 at 628-29 (2d ed. 1955).

[15] E.g., *Krebs* v. *McNeal*, 222 Miss. 560, 76 So.2d 693 (1955).

its member or by supplementing the information known to the Institute. It would probably, however, be appropriate to bring the information to the attention of the Iowa society, if the fact of the accountant's Iowa residence indicates his probable membership in that society,[16] or that the society would be a likely source of complementary information, whether exculpatory or inculpating.[17]

Also, information known to the Institute, contemporaneously or subsequently acquired, that tends to clear or exculpate an accountant reported upon should be forwarded promptly to those organizations which have received information adverse to the same accountant. Not only would such a routine course of action tend to establish the reasonableness necessary to a qualified privilege, while serving as well to lessen injury and damages, but it would also effect a proper regard for the individual concerned.[18]

Conclusion

We are persuaded that, because the public and professional welfare are served by the enforcement by the accounting profession of high ethical standards, and because a strong common interest is so readily apparent among the organizations concerned, qualified privilege should effectively shield the Institute from legal liability for defamation arising from the proposed program of exchange of disciplinary information. There should be reasonable restraint, preliminary verification where practicable, and some care to avoid circumstances supporting a charge of bad faith. Should unusual circumstances appear, the Institute should consult legal counsel.

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[16] *Restatement* Sec. 596, *Comment c.*

[17] Consent could provide an additional defense. The *Restatement* (3 *Restatement, Torts* Sec. 583, *Comment f*) indicates that plaintiff's consent confers upon defendant, so long as he stays within its scope, an absolute privilege immune to defeasance even on a showing of malice. Prosser, too, catalogues consent as conferring an absolute privilege. Prosser, *Law of Torts* Sec. 109 (3d ed. 1964). Harper and James (1 Harper & James, *Law of Torts* Sec. 5.17 (1956)) set out what on balance seems a more sound position: that consent confers a qualified privilege defeasible by the establishment of malice. Cf. *Developments in the Law—Defamation*, 69 Harv. L. Rev. 875, 931-32 (1956). The utility of consent, as an additional defense for the Institute, would depend upon further modification of the bylaws and membership application forms, unless it were obtained directly from the accountant concerned.

[18] See *Whitcomb* v. *Hearst Corp.* 329 Mass. 193, 107 N.E.2d 295 (1952); Prosser, *Law of Torts* Sec. 111 (3d ed. 1964); Harper & James, *Law of Torts* Sec. 5.30 (1956); *Developments in the Law—Defamation*, 69 Harv. L. Rev. 875, 940-42 (1956).