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Milestones in the History of Public Accounting

Robert G. Allyn, CPA

The history of public accounting is marked with many interesting and notable milestones. Public accounting may lack the glamor and the kind of intimate and personal relationship with all members of the community, which is enjoyed by certain other professions, but public accounting, nevertheless, has had a long history featured by several outstanding events. A few of these events are recounted briefly in the following paragraphs.

Accounting, or perhaps it would be more correct to say bookkeeping, in its earliest development was of little significance in economic affairs until capitalism became the characteristic and dominant economic force in the political economy of the great nations of the world. Prior to that time, economic life generally was characterized by production for use instead of by exchange. Werner Sombart, the eminent historian of capitalism, describes the pre-capitalist period as one wherein the "idea of sufficient livelihood for each class in accordance with needs was 'the governing conception.'"¹ The craftsmen of the medieval period were mainly preoccupied with providing themselves and their families with a sustenance in accordance with the "needs of their station."² As a result, medieval arithmetic and accounting were often incorrect and approximate when applied to financial data.

In an earlier age, the Hindu-Arabic numerical system was invented, but it was many centuries before this system of numbers as we know it supplanted the more commonly-used Roman numeral system. Evidence of the Roman numeral system is to be found in use in commercial affairs as late as the 17th century. Arabic numerals were resisted in the conduct of commercial activities because banks, for one reason, objected that their use made forgery easier than Roman numerals.³

The decline of the feudal system, the creation of the European nations, the commercial revolution of the 15th and 16th centuries, a sharp increase in population following a decimation of the population due to pestilence in the latter middle ages, the Industrial Revolution of the 18th and 19th centuries when the highly individualized craft system gave way to the factory system, the abandonment of mercantilism as the mainspring of political economy in favor of a laissez-faire economic policy—these were some of the main factors contributing to the development of capitalism.

"The beginnings of well-ordered bookkeeping stretch back into the 13th century."⁴ It was not until 1494 in Venice that the first treatise on bookkeeping was written. "The author was one of the most celebrated mathematicians of his day. . . ."⁵ His name was Luca Paciolo, a member of the order of St. Francis. He describes himself as a humble professor of theology. Paciolo, however, was clearly familiar with mercantile affairs largely through his services as a tutor to the sons of one of the merchant princes of the Republic of Venice. Interestingly, his chief work was entitled, "Everything about Arithmetic, Geometry and Proportion." Paciolo attempted to summarize the existing knowledge of mathematics in this opus. At the conclusion of the work on arithmetic, he interjected a treatise on double-entry bookkeeping. Of this work he said, "In order that the honourable subjects of the most gracious Duke of Urbino may have complete instructions in the ordering of business, I have decided to go beyond the proposed scope of this work and add this most necessary treatise."⁶

It is difficult to establish a time when public accountants first made their appearance in the economic affairs of the community. As a profession, public accounting was recognized for the first time in Scotland. "The first professional accountant in Scotland of whom we have been able to discover any trace is George Watson . . . born in Edinburgh in 1645 . . . died on 3rd April 1723."⁷

Alexander Chalmers was another early accountant who might be described as "public." "When the Church of Scotland in 1744 established a Fund for the Widows and Orphans of its Ministers, Mr. Chalmers was employed to prepare a table of interest. . . . for which he was allowed £3, 3s."⁸ Later in this same connection, Chalmers examined the calculations upon which the contributions were made. He commented that they were "every way just and as well founded as the nature of the thing will admit."⁹

The first step toward the formation of a society of public accountants took place in January 1853 when 14 practitioners in Edinburgh were invited by one of their members to form an association to unite the profession.

In England the earliest accountants of which there is any record were teachers of bookkeeping and keepers of accounts.¹⁰

In the United States, the American Association of Public Accountants was incorporated under the laws of New York State on August 20, 1887. At its first annual meeting in May, 1889, the Association numbered 25 Fellows and 7 Associates. In 1892, the Association started a school of accounts in New York City, but the school proved to be a failure. Prior to this date, in 1881, through the benefaction of Joseph Wharton, the Wharton School of Business was formed at the University of Pennsylvania. This was the country's first business school. In the deed of gift it was provided that the faculty should include "One professor or Instructor of Accounting or Bookkeeping, to teach the simplest and most practical forms of bookkeeping for housekeepers, for private individuals, for commercial and banking firms, for manufacturing establishments and for banks. . . ." ¹¹ In 1900, the New York State Society of Certified Public Accountants was instrumental in establishing the New York University School of Commerce, Accounts, and Finance. These were the first instances when accounting was taught on a collegiate level.

An Act to regulate the profession of public accounting in New York State was passed by the legislature on August 17, 1896. This was followed by similar legislation in Pennsylvania (1899), Maryland (1900), California (1901), Illinois (1903), Washington (1903) and New Jersey (1904). Presently all 50 states have some legislation which defines public accounting as a profession and regulates the entrance into the profession and its practice. In New York State, public accounting is one of 20 professions legally defined and regulated by the Board of Regents and the Department of Education.

Auditing is now recognized as a principal service performed by the public accountant. In rendering this service, he is looked upon as an independent practitioner and an expert in the knowledge and application of accounting principles and auditing standards. Accordingly, his expression of an independent judgment upon the financial statements and the operations of those enterprises which make up his clientele is highly respected. Legally, the public accountant is held responsible in courts of law for his failure of omission or commission in applying auditing standards or in the adherence to recognized accounting principles in the conduct of an audit. This is a recent innovation in the long history of bookkeeping and accounting.

The ancient Egyptians, Greeks, and Romans required checks upon the activities of public officials, by requiring, for instance, that receipts be recorded separately by two officers. In Ancient Greece when an official left his

office, his accounts were ordered to be examined. ¹²

A kind of bookkeeping technique with a unique control feature employed as late as the 17th century principally in England was the tally. The tally was a notched stick made usually of hazel wood. Cuts or notches were made in the stick to represent various denominations of currency. These cuts ranged in size from the palm of the hand, to the breadth of the little finger, to a grain of barley, or to a slit. After the stick was notched, it was split almost throughout its length, leaving a small end or stub at the end of one of the halves. This half was called the stock; and when the tally was used as a form of receipt, it was retained by the creditor; the other half or foil was given to the debtor. It was not until 1826 that the use of tallies was finally abandoned by the Council of the Exchequer. The tallies were ordered destroyed by King William IV in 1834. The intensity of heat caused by the burning tallies resulted in the Parliament buildings being burned to the ground. ¹³

It was not until the 20th century that auditing received official sanction. In 1900 the Companies Act in England was amended to provide for audits by public accountants of limited companies. Three decades later, the then American Institute of Accountants (now the American Institute of Certified Public Accountants) Committee on Cooperation with Stock Exchanges issued a report September 22, 1932 to the New York Stock Exchange.

"This scheme contemplated an adequate disclosure by listed corporations of the methods of accounting employed by them and an undertaking not to make any material change either in the methods themselves or in the way in which they were applied, without full disclosure to the Exchange and to stockholders. The independent auditors were to be charged with the responsibility of reporting whether accounts were in conformity with the representations made." ¹⁴

Although the pronouncements of the American Institute were not official in that they were legally mandatory, they did demand compliance from a large percentage of the profession particularly the members of the Institute who make up the major group of public accountants in the United States. Since that date many states have incorporated the provisions of full disclosure and compliance with auditing standards and accounting principles in the statutes of professional conduct thereby mandating an adherence to the standards developed by the profession and to be found in the pronouncements of the Institute.

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COMMENTS AND IDEA EXCHANGE

JANE STRENCIWILK, CPA

Reporting of Unpaid Wages for Workmen's Compensation

The Industrial Commission of Arizona (Workmen's Compensation agency) has ruled that nonpayment of wages to an officer of a corporation does not relieve the Commission of liability. Therefore, they require reporting of wages and payment of insurance premium even though no wages are actually paid.

This ruling was derived from a recent suit against ICA, in which the courts awarded compensation to the estate of an officer who had not been receiving or reporting salary, but who had been actively working in his business and was therefore considered to be in covered employment.

Since the Corporate minutes should specify whether or not such an officer is to be paid, and how much salary he is to receive, the minutes govern the amount to be reported. If the minutes contain no mention of salary, or if he is to be paid a per cent of profit, then he is not covered because no specific amount can be determined.

Many such officers may prefer to have or retain coverage, even though they forego the salary on which it is based. This ruling makes such a step possible.

Any employee who chooses to do so, officer or not, may reject the terms of the Arizona Workmen's Compensation law by turning in a special rejection slip.

Kit Paxton

Tucson ASWA Chapter No. 58

CLIENT INFORMATION PINKY

Reporting information to the federal and state government daily grows more complex, particularly for the layman who is unfamiliar with the standard forms and procedures used. Governmental agencies seem to change forms as often as women change hair-do's, so it is not surprising that even the most knowledgeable employer preparing quarterly returns, or individuals or business firms preparing income tax returns, have difficulty with minor details.

To facilitate the filing of forms prepared in our office, and to eliminate the possibility of client error, we use a "Pinky"—a pre-printed, pink form which is attached to material sent to the client for final disposition.

EXAMPLES

Income Tax Returns

Corporations: Forms 1120, 120 and the Corporation Commission Report each have a pinky attached which indicates who should sign, where to sign (the red X marks the

spot!), what checks are needed, to whom they are payable, and the due date for filing. In addition, it will explain to the client what he is paying (i.e. on the federal return he may pay *all* or 50% of his tax liability when the return is filed. If he pays 50% it explains about later billing for the balance due.) The client is instructed to affix the corporate seal, sign his name, title, and date.

Partnerships: Basically the same information is covered, with the exception that there is no provision for payment since no payment is required at the time of filing.

Individuals: A pinky is attached to Forms 1040, 140, and the client's declaration of estimated tax, explaining, in detail who is to sign, where to sign, dating the returns, and due date for filing. It explains fully what checks are necessary and to whom payable, or if no payment is required. If a refund is due, the pinky tells the client if he will receive refund or if it is applied to his estimated tax for the coming year.

Payroll Tax Reports, Sales Taxes and Miscellaneous Forms

The pinky informs the client as to what form has been prepared for him. Again, the place for signing is indicated in red, the due date is specified, and the correct name of the agency to whom the check is payable is listed.

As a courtesy to the client, and also as an added error preventative, stamped, addressed envelopes are attached to each form. Copies to be retained by the client are clearly stamped "Client Copy." There are times when, in addition to the pinky, it is necessary to write a covering letter to specify in greater detail what has been done and what still remains to be done, but generally the pinky will be sufficient.

Ellen R. Butler

Tucson ASWA Chapter No. 58

Milestones

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The passage of the 16th Amendment to the Constitution in 1909 and its ratification by the states in 1913 is another milestone in the history of public accounting. The preparation of income tax returns has become a significant part of the services rendered by the profession. In this area, two problems have assumed considerable importance. One is the reconciliation of the determination of net taxable income, computed in accordance with the Internal Revenue Code and the Regulations of the Internal Revenue Service, with the determina-

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TIPS FOR BUSY READERS

MARY J. McCANN, CPA

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"Change of Accounting Method Versus Correction of Error," Jack Macy, *The Journal of Accountancy*, November 1964, Volume 118, Number 5.

A myriad of cases, followed closely by *Revenue Procedure 64-16, 1964-9 IRB 35*, makes the reading of this article a "must." Revenue Rulings concerning the treatment of vacation pay accruals, coupled with Presidential concern in 1961 of tax abuses within the inventory area, have given rise to substantial litigation predicated on changes in accounting methods.

The author carefully traces the development of Treasury Department examinations through the review of pertinent cases. He points out the fine line of distinction that is being drawn between corrections of errors and outright changes in accounting methods. It is important to note that under Regulation 1.481-1(a)(2) where a change in accounting method results in additional income, the portion of the adjustment applicable to periods prior to January 1, 1954 escapes taxation, *provided the change is initiated by the Commissioner*. On the other hand, if the taxpayer originates the change, the entire amount of income resulting therefrom is taxable. As a result of the stalemate that must arise under these circumstances, Mr. Macy discusses the partial relief afforded by *Revenue Procedure 64-16, supra*. Under this procedure the taxpayer may request a change in accounting "practice" which permits any increases in income to be spread over a ten-year period, beginning with the transitional year.

Those paragraphs dealing with corrections of error are most revealing. Almost every business, regardless of size, is guilty of at least one of the enumerated mistakes. As accountants, therefore, we should be familiar with the faults that are presently under surveillance, the tax consequences of their correction, and the possible conflict between Sections 1311-15 and 481 of the Internal Revenue Code. A

study of these sections alone will not supply us with the answer, and it is for this reason Mr. Macy's article is recommended for your "required reading" list.

D.L.B.

"Some Aspects of Measurement and Accounting," Hector R. Anton, *Journal of Accounting Research*, Spring 1964, Volume 2, Number 1.

In this rather technical article, Mr. Anton compares the requirements for an effective accounting system with the basic properties of a military command-control system.

He discusses the fact that systems require input of data, but output of information. He arrives at a five-part process for measuring the information which is the end-product of the accounting system. The five parts are independent actions but form one integrated process.

He concludes the article with the thought that accountants have done relatively little in testing efficiency of information relative to its cost although much time has been devoted to the problems of generating and processing data. This article points out the need for additional research in the areas of (1) data language, (2) data specifications, (3) data standardization, and (4) data accuracy and control.

M.E.D.

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tion of net income arrived at in conformity with generally accepted accounting principles. Another problem facing the profession is the achievement of an understanding and a modus operandi with the Revenue Service with respect to the extent of responsibility and liability of the public accountant in the preparation of tax returns for clients. This problem appears to have been reasonably worked out in England and on the continent but not in this country. A solution in this country would be another milestone of significance.

The most recent milestone in the history of public accountancy has been the passage by the various states of legislation to license or register all practicing public accountants, hitherto restricted to those who met the requirements to become certified public accountants. Legislation providing for the enrollment and registration of public accountants (not certified) was passed in New York State in 1959. In 1963, there were about 16,000 cer-

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EDITOR'S PAGE

This publication seeks to publish articles written by our two sponsoring organizations, the American Woman's Society of Certified Public Accountants and the American Society of Women Accountants.

"Cursory Exploration of RPM of Business Records" was submitted by Mrs. Thelma Barkley, a member of the Birmingham ASWA Chapter. Mrs. Barkley submitted an outline, which we are not publishing, but which explains the "RPM" in her title as follows:

- "R"—Retention of business records***
- "P"—Preservation of business records***
- "M"—Microfilming"

We anticipate that a number of the members of our two sponsoring organizations will find this article to be quite useful.

The article "Bowling Center Operations" written by Mrs. Kit Paxton, member of the Tucson ASWA Chapter, is an example of "if you don't at first succeed, then try again." Sometime ago, Mrs. Paxton submitted an article with the same subject. In the opinion of members of the Editorial Board, who re-

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tified public accountants and 8,500 public accountants registered to practice.

To conclude this brief and subjective history of the profession, it may be well to consider another milestone that the profession may have to face and with some apprehension. This is the effect of "creeping socialism" and the effect it may have upon the independence of the members of the profession. The increasing participation in business activities by the Federal government either as an owner and operator or as a regulator through the growth of agencies that impose controls through standards, setting of rates, and so on, while it may well lead to an increased demand for accounting services, may at the same time affect the independent judgment of the public accountant. Public accounting has made rapid strides in an economic setting marked by relatively free enterprise; it may be retarded in an economy less free and closely regulated. Paton has expressed concern for this trend very cogently:

"Under socialism accounting procedures are almost sure to be rigidly prescribed, permitting little or no room for the application of professional analysis and judgment. With government completely in charge, progress in accounting theory and procedure will tend to cease, and accountants—although they may be numerous and very busy—will tend to revert to a clerical status."¹⁵

viewed the article, it was not suitable for publication. Thereafter, certain suggestions were made to Mrs. Paxton, who rewrote her article and resubmitted it. We believe that our readers will find it quite interesting and perhaps, in some instances, useful.

At the 1964 Joint Annual Meeting of AWSCPA—ASWA, much recognition was given to Tucson ASWA Chapter No. 58. Readers will recall that that Chapter received the AWSCPA award for the year ended June 30, 1964. It would appear that the same Chapter is making a concerted effort to repeat its performance of the past year. Your editor was pleased to receive material for the Comments and Idea Exchange from Jane Strenciwilk, editor, which consisted of two items submitted by Tucson members, Kit Paxton (see our comments above) and Ellen R. Butler. Perhaps this will serve as encouragement to other ASWA Chapter members to submit material for the Comments and Idea Exchange, as well as for the Tax Forum.

Milestones

(concluded)

This may serve as a challenge to the profession to continue to maintain high standards as a kind of bastion in the protection of its independence which is the keystone of the profession.

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²*Ibid.*, page 16.

³Newman, James R. ed. *The World of Mathematics*, vol. 1, Simon and Schuster, 1956, page 451.

⁴Sombart, *op. cit.*, page 127.

⁵Brown, Richard, *A History of Accounting and Accountants*, Edinburgh, T. C. & E. C. Jack, 1905, page 108.

⁶*Ibid.*, page 109.

⁷*Ibid.*, pages 183-185.

⁸*Ibid.*, page 186.

⁹*Ibid.*, page 186.

¹⁰*Ibid.*, page 232.

¹¹Pierson, Frank C. and others, *The Education of American Businessmen*, McGraw-Hill Book Company, Inc., N.Y. 1959, page 355.

¹²Brown, *op. cit.*, page 74.

¹³Littleton and Yamey, *Studies in the History of Accounting*, Richard D. Irwin Inc., Illinois, 1956, page 85.

¹⁴May, George O., *Financial Accounting*, The Macmillan Company, N.Y., 1943, page 56.

¹⁵Paton, William A. "ACCOUNTING AND UTILIZATION OF RESOURCES," *Journal of Accounting Research*, Vol. 1, No. 1 Spring, 1963, published by the Institute of Professional Accounting, Graduate School of Business, University of Chicago, and the London School of Economics and Political Science, page 46.