

3-1939

Serving a Public Need

Philip A. Benson

Follow this and additional works at: <https://egrove.olemiss.edu/jofa>



Part of the [Accounting Commons](#)

Recommended Citation

Benson, Philip A. (1939) "Serving a Public Need," *Journal of Accountancy*. Vol. 67: Iss. 3, Article 4.
Available at: <https://egrove.olemiss.edu/jofa/vol67/iss3/4>

This Article is brought to you for free and open access by the Archival Digital Accounting Collection at eGrove. It has been accepted for inclusion in Journal of Accountancy by an authorized editor of eGrove. For more information, please contact egrove@olemiss.edu.

Serving a Public Need

BY PHILIP A. BENSON

I FEEL greatly honored to be your guest on this occasion. Knowing how busy accountants are at this time of year it is a pleasure to note that so many of you have been willing to take the time to attend this dinner and make this such an enjoyable evening for me. I take pride in the fact that I have been a member of your profession and a member of the New York State Society of Certified Public Accountants for more than twenty-five years.

During these twenty-five years we have seen great changes, both economic and political. These changes have affected profoundly both your business and mine. Many of the developments have inured to your benefit, for they have increased the demand for your professional services. Many business concerns that did not employ auditors and accountants (except perhaps those on their own pay roll) have, because of the growing complexities of business and of governmental requirements, found professional accounting services a necessity. Perhaps taxation in its various forms most clearly illustrates this. We have taxes today that were not thought of twenty-five years ago; in fact, our first federal income-tax law went into effect about that time. Since its inception we have had a succession of federal and state laws imposing income taxes, surtaxes, excess-profits taxes, capital-gains taxes, etc. The detailed provisions of these laws have been numerous and varied. It is interesting to note that twenty-five years ago the burden of taxation for the entire nation—national, state, and local—

NOTE.—This paper was presented by Mr. Benson at a dinner given in his honor by the American Institute of Accountants and the New York State Society of Certified Public Accountants at the Waldorf-Astoria Hotel, New York, N. Y., January 30, 1939.

amounted to about two billion dollars and last year it was thirteen billion dollars. I do not know what the national income was in 1913, but I do know that the taxes then were a small percentage of it. Last year taxes took 20 per cent of our national income. While your work has been greatly increased by the large volume of tax legislation, the country has had to shoulder the burden of paying the tax and this becomes a heavier burden year by year, and one that rests on all classes of people.

Your profession is the outgrowth of the industrial revolution that commenced about 160 years ago and of the development of the corporation as a business entity by means of which millions of people invest their savings. Of course, all business is not carried on in the corporate form, but a great deal is, and these corporations engage in every variety of business activity.

For a while, in the minds of some people, business was considered evil and businessmen were held up to ridicule and scorn. The idea sprang from ignorance and prejudice. Fortunately, as is the way of all things false, this conception did not last long. Business, as I have described it, provides a living for everyone. It is a boon and a blessing. It must be carried on; it should be encouraged. But because we believe in free enterprise, control and operation of business must be in the hands of those who own it and not of the state.

PROFESSIONAL RESPONSIBILITY

Your business is accounting, mine is banking. Your business is truly a profession. You practise under a code of professional ethics and you seek primarily to render a service to your clients. The remuneration is incidental. You, as a profession, have a code, but

Serving a Public Need

that does not mean that your standards are higher than those of banking or of any business you serve. All business is coming to realize more and more that it must be conducted on the highest standards, and that it has social responsibilities.

Among the duties of executives is the responsibility of seeing that a proper accounting record is made of all transactions and occurrences affecting their business. In a large office there will be accounting officers with a staff and machinery to do this. These employees work under the executive officers, however, and are directed by them. From time to time the officers want to know that the records of the business that have been kept are honest records and that they are complete. They want to have before them statements of the operation and condition of the business and require that these statements bear a certificate attesting to their truth and accuracy signed by someone whose professional skill and accuracy as an accountant is recognized. These executives are the management, and management must have the information and the assurance that your reports provide.

Not only management but the many others, directors, stockholders, and creditors, interested in a business rely on the work you do, and this places a grave responsibility upon you to protect them and safeguard their fortunes.

Directors have a special reason for employing professional accountants and relying upon their work. Directors are elected by stockholders and represent the proprietorship in the business. The responsibility of directors to "direct" is becoming more widely recognized. Directors may attend a hurried meeting, listen to a few remarks and reports by the presiding officer, pass a resolution, such as the declaration of a dividend, and leave the meeting. They have not thus altogether discharged their duty, however. They should inquire how the business is being conducted,

what have been the results and what is its condition. I know the difficulties the average director has to get all the information needed in the short time available. For this reason I believe the management should see that every director is furnished with frequent statements, in sufficient detail, in order that he may know as much as possible of the business he is directing.

Your responsibility as accountants extends to the stockholders of the company. Your reports inform them of the progress of their business. Many of these stockholders are not business people. Every statement in your reports that reaches the stockholders should be clear. The stockholders should be able to see by reading it just what you have done and what, if anything, you have *not* done with respect to the figures presented. Management no doubt is thoroughly familiar with the way you have done your work and the extent of your verifications. Directors should possess the business acumen and judgment necessary to observe the same things in your reports. But the public—that is another story, and you have undoubtedly a definite responsibility to protect the investing public.

SOME PROBLEMS OF ACCOUNTING

In carrying on your work you have many difficulties and problems. For example, if you are examining a bank with thousands of small depositors, how can you be sure that the books reflect the true deposit liability? Verifying every balance by correspondence would be practically impossible and, in many ways, not desirable. However, you have ways of making test checks that will satisfy you that the depositors' accounts correctly reflect the liability.

There are difficulties in the way of ascertaining the amount due on each mortgage in a large mortgage portfolio, and yet enough test checks can be made to satisfy you that the total *is* correct. However, we must realize that at times

a smart crook can fool even a good accountant!

The matter of inventories has been discussed in the newspapers recently and it is a subject, I presume, that has given accountants a great deal of anxious thought. What, then, is your responsibility with regard to certifying to inventories? Inventories in some concerns include raw materials, goods in process, and finished goods, often located in many different and sometimes widely separated places.

What you do with respect to inventories will, of course, depend largely on the terms of your engagement. You may not be expected to verify them at all. On the other hand, a complete verification may be required.

I know that, if you had any idea that instructions to omit checking inventory were for the purpose of concealing a fraud or inflating assets, you would refuse the engagement. However, we all know that fraud or deceit of this kind is a very rare occurrence and that there is usually no reason to refuse to make an audit, excluding inventories. You know that your report will be used primarily by the officers and directors of the business, who know or should know what instructions were given you. On the other hand, your report may be read by stockholders and creditors and other investors, and special safeguards should be taken to protect them against fraud. If inventories and certain other assets are not verified a clear and unequivocal statement to that effect should have a prominent place in your report.

The resolution adopted by the New York State Society on May 10, 1934, clearly defines the responsibilities of the accountant with respect to this matter of inventories:

"Resolved, That it is the sense of the New York State Society of Certified Public Accountants that, if a certified public accountant reports on a balance-sheet of a concern over his signature without qualification or special explana-

tion as to the item of merchandise inventories contained therein, it shall imply that he has exercised care in his examination by making accounting tests and checks of the concern's books of account and other available records pertaining to merchandise inventories, that he has received all information and explanations he has required from the officers and employees responsible for the taking and valuation of the merchandise inventories, and so far as accounting methods permit, has satisfied himself as to their substantial correctness, but that, as regards the information and explanations he has required and as to ownership, physical quantities, description, quality, condition, marketability, and valuation of the merchandise, he has relied upon the representations of the concern's management, subject to such checks as may have been obtainable from the records in respect thereto."

When a business enterprise fails either through sudden and unforeseen economic changes or through the manipulations of a dishonest, though clever, official, not only is there general amazement that such a thing could happen but there is public clamor for a scapegoat. Discussion in the public press of a recent celebrated case takes accountants to task and raises the question as to the accuracy and completeness of the auditing and accounting procedure that had been followed. Those who discuss the case make many impractical suggestions to prevent recurrence. Worst of all, an ill-deserved shadow of a cloud falls upon a great profession.

ACCOMPLISHMENTS OF THE PROFESSION

It would be unfortunate if the public failed to recognize what the accounting profession has done to raise the standards of accounting in this country. It would be unfair and unjust if clamor and criticism should so becloud the public mind that the record of achievement, during more than forty years, of your professional societies in promoting high ideals and establishing the most efficient

and desirable methods of accounting and reporting should be forgotten. It has not been easy to accomplish what has been done, but you have had great leadership and you have all followed this lead to higher ground during these years.

To prove this, let us look at the record. Read, if you will, the published reports of corporations over the period of the last ten to twenty years and note the progressive improvement. Study accounting methods in financial and commercial concerns, including cost accounting, and observe that it has steadily become more scientific. The profession throughout the world awards first place to your work for its quality, and you can be justly proud of the esteem in which it holds you.

Let it also be said to your credit that, as you have raised your own professional standards, so have you raised the standards of business generally, and full disclosures in annual reports are accepted practice.

Progress in accounting and auditing has been accomplished in spite of many difficulties and some opposition. A peculiar difficulty that you face constantly is the fact that in the eyes of the public, of management, of directorates, and often of the courts you have a serious responsibility, yet you are denied the authority to demand compliance with your proper requirements. There do not seem to exist enough definite statutory enactments which give the auditor powers which should accompany his responsibility. In the public interest, this should be remedied. At the same time, your own past record gives assurance that your two bodies will continue to study present auditing and accounting practices and procedure and to introduce whatever improvements may be suggested.

The public is entitled to be fully assured regarding the integrity of all published statements bearing a professional certification.

THE NATURAL BUSINESS YEAR

In these days when every effort is being made to protect the investing public, when the accuracy and completeness of accountants' examinations and reports are essential to so many people, it seems desirable to take whatever steps may be required to expedite the work and eliminate whatever is unnecessary. Suggestions have been made, among them being two that seem particularly desirable. The first is that to a greater extent the natural business year be used for fiscal purposes rather than the calendar year. This will have the effect of spreading the work so that there will not be such a tremendous rush to complete reports following the end of the calendar year, and will permit corporations to close their books at the end of the natural cycle of their operations. I am sure you are familiar with the suggestion, so I am merely stating my belief in the principle.

The second suggestion is included in a memorandum submitted to the United State Treasury Department by our committee on federal taxation. This report contains a statement that "the determination of fixed principles of federal taxation should strive to bridge the existing gap between tax accounting and established commercial practice."

Adoption of this suggestion and some of the others contained in this very excellent memorandum would help to simplify the making of tax reports for all businessmen and their accountants.

Much could be said in favor of having accountants and auditors designated by the board of directors and of having reports made directly to the board. It has also been suggested that the accountants be elected by the stockholders at their annual meeting. This would be helpful, especially if it were required that, if any change in the accounting firm were contemplated, the notice sent to the stockholders report such a contemplated change. This would put

stockholders on notice, and if they so desired they could appear at the meeting and learn the reason for the change.

THE AMERICAN BANKING SYSTEM

Many of our banks are among your clients, and the American Bankers Association itself has benefited by the valuable services of some of your members. Moreover, banking is the servant of all your clients.

When we speak about our American banking system, we realize that it includes all the banks chartered by the federal government under the national banking act and those chartered by the forty-eight separate states. Our system includes Federal Reserve Banks which were created about twenty-five years ago. These are banks of rediscount. They also furnish the larger part of our currency, which incidentally is backed by gold with the United States Treasury. Another way of describing our banking system would be to say that it includes commercial banks, trust companies, and savings banks. Many banks, however, perform all three functions. We might say, also, that there are unit banks, that is, banks with no branches, and banks with branches, some with few and others with many. Our unit banks are in the majority. These banks have served their communities well and are opposed to any extension of branch banking that would threaten their independent existence.

The resources of our banks at the present time are over 68 billions of dollars. Many of these banks are members of the Federal Reserve System and are required to keep a reserve with a Federal Reserve Bank. At the present time these reserves are more than three billions of dollars in excess of legal requirements.

Of one thing I can assure you, and that is that our banks are stronger and more efficient than they have ever been in the country's history. It would not be an exaggeration to say that our banking system is the best in the world.

What banks lack, however, are earnings. Interest rates are low and the item of loans and discounts, which formerly meant so much of a bank's earnings, is very much smaller than it used to be.

Bankers and accountants have a natural community of interest. We are complementary to each other. So complex has the business and credit life of the country become that it is largely through the services of such men as you that the extension of credit service to business is facilitated.

A soundly prepared and properly certified financial statement lies at the heart of all credit extensions. It is practically the first requirement expected of any borrower, and the extent to which bankers depend on such statements is a tribute to the ability of the accounting profession.

CHANGES IN BANKING METHODS

It is true that loans are not being made in the same volume as they were in happier days. It is true that the character of commercial banking seems to be undergoing a change. But the change is one that bankers would avoid if they could. The training of bankers has been predominantly in the field of commercial credit, and loans have been the lifeblood of banking. Lending money, rather than investing money, has been the essence of American banking. Investing activity has been an incidental form of banking life. Fifteen years ago three-fourths of the assets of banks represented loans to business and one-quarter represented investments. Today less than one-half of the assets of banks are in loans and more than one-half in investments.

I have said that a change seems to be coming over the character of the banking business. The plain fact is that business and industry do not desire bank credit to the extent they once did. In the late twenties corporations with access to the security markets found it convenient to raise necessary working

funds through the sale of stock to the public. This operation involved no obligation of repayment and no interest rate beyond the dividends to be paid, if and when earned. In addition, these and many other corporations increasingly pursued the practice of accumulating reserve funds out of earnings for use in their operations and capital expansions. Today they continue independent of the banking system, to a considerable degree, for working capital requirements.

A second influence in reducing the need for bank credit has been the great speeding up of transportation facilities and manufacturing processes. Traditionally bank credit was used to finance the acquisition of large quantities of raw materials for processing into finished goods. In many industries large inventories are a thing of the past. So rapid are deliveries and production processes that businesses no longer have to take advance delivery of their entire seasonal requirements. The manufacturing and merchandising process has been made a more continuous process, with current sales tending to finance new orders.

Today the banks seem on the way to becoming investment institutions rather than lending institutions. And this by reason of alteration in business practice and government policy.

Our banking system was not evolved to meet the kind of demands that are now put upon it. It grew up to serve the commercial needs of the country. It consists for the most part of a far-flung system of locally owned community banks whose traditional activity was the use of local funds in financing the life and the development of the local community. It played a magnificent part in the conquest of this continent and the establishment of the American civilization.

A third influence has been that of the federal government. Its policies have acted as a general deterrent to the prog-

ress of business and therefore to the need for credit. It has loaded the banks with investments in the form of government bonds. And it set up an increasing number of credit agencies, in direct competition with banks, which have taken a considerable volume of lending business away from banks.

In passing, it might also be remarked that the cheap money conditions created by governmental policy have made it extremely difficult for banks to make livable earnings. It has forced them to make loans at low rates at a time when their overhead is steadily increasing and idle deposits are piling up as a result of government spending. Since their traditional forms of earnings are being reduced, banks are forced to employ their funds more largely in bond investments.

Thus we see two tendencies at work, one a declining demand for bank credit and the other, a result of the first, a shift in the employment of bank funds from credit to investments. How permanent this shift will be only time will tell.

NEW BANKING SERVICES

You might ask, "If the scope of banking has been restricted by the changes indicated, how is the American system of community banks now serving the public?"

Under the pressure of the need for earnings and for self-preservation, I think it may be said that banks are taking on a somewhat broader character. Instead of serving only the commercial needs of their territories, they are taking on the character of institutions serving the general financial needs of their communities.

A year ago a popular banking magazine published a list of the separate services rendered by banks to the public. These aggregated no less than forty, and ran practically the whole gamut of financial need—business, family, and personal. Bankers are not saying much about it, but they are engaged to a very

considerable degree in the development of what they call "term loans," or "intermediate credit." Many banks are making such loans to established business enterprises. These loans run from two to five years, and in some instances even ten years. Banks have adapted to their use the amortization principle now recognized in the mortgage field, and make this form of loan under terms that extinguish it by the time of its maturity. This is but one of the ways in which banks are trying to meet the new credit requirements of business. Of course they still make and constantly seek the short-term loans that have always been the principal service of commercial banking.

Real-estate financing has taken on a new importance in banking. An entirely new system of mortgage financing has been evolved, and large sums have been advanced to home owners and other owners of real estate property. This has been beneficial both to the borrowers and to the banks. Today, when a prospective borrower applies to a bank for a real estate loan, he is asked to subscribe to a plan, adapted to his financial status, under which he will regularly amortize his loan and own the property free of debt at the end of the mortgage period.

No longer is it necessary for people seeking personal credit to obtain it at excessive rates of interest from agencies of distant lending corporations. Today in practically every community residents with satisfactory records of employment may obtain personal loans for needful purposes or for the purchase of automobiles and household equipment at moderate rates of interest.

Perhaps the newest personal service of banks consists of the checking services designed to extend to everyone the convenience of payment by check. Not so long ago a person had to maintain a certain minimum balance in order to have a checking account. This put the service beyond the means of many

people. Nevertheless, checking-account service became a personal convenience in this country to an extent far greater than in any other country. Now banks in every section of the land are establishing "no minimum balance" checking-account systems under which one simply pays for what he gets. He gives the bank the amount of money he wants to transfer and simply pays a fee for the check or checks he uses to transfer it.

THE AMERICAN BANKERS ASSOCIATION

The American Bankers Association, of which I am president this year, is the focal point in the development of broadened banking service to the public. It is a vast educational organization. It sponsors the largest organization in the world devoted to adult education—the American Institute of Banking, inaugurated forty-three years ago by a group of bank employees who desired to learn more about their chosen business field. It sponsors also the Graduate School of Banking. Six hundred bank officers are enrolled in this school.

But the educational activities of the Association do not stop there. Each winter the Association conducts a series of three regional banking conferences in three different sections of the country. These are courses in current banking problems, and usually draw from 1,000 to 1,500 bankers who go to school in six intensive sessions, morning, afternoon, and evening for two days.

This winter we plan to hold one of these conferences in New York. It will be devoted to the theme of "Meeting the Public Needs in Banking."

The American Bankers Association recognizes that, while political and social forces may modify the practice of banking, the future of banking is the measure of its service to the public.

Is it not true that the future of your profession also depends upon the measure of your service, and that improving and increasing such service may well be a plank in your own platform?