University of Mississippi
eGrove

Guides, Handbooks and Manuals

American Institute of Certified Public Accountants (AICPA) Historical Collection

1970

Rise of the accounting profession, v. 2. To responsibility and authority, 1937-1969;

John L. (John Lansing) Carey (1904-1987)

Follow this and additional works at: https://egrove.olemiss.edu/aicpa_guides

Part of the Accounting Commons, and the Taxation Commons

Recommended Citation

Carey (1904-1987), John L. (John Lansing), "Rise of the accounting profession, v. 2. To responsibility and authority, 1937-1969;" (1970). *Guides, Handbooks and Manuals*. 31.
https://egrove.olemiss.edu/aicpa_guides/31

This Book is brought to you for free and open access by the American Institute of Certified Public Accountants (AICPA) Historical Collection at eGrove. It has been accepted for inclusion in Guides, Handbooks and Manuals by an authorized administrator of eGrove. For more information, please contact egrove@olemiss.edu.

The Rise of the Accounting Profession

To Responsibility and Authority

1937-1969

John L. Carey

The Rise of the Accounting Profession

The Rise of the Accounting Profession

To Responsibility and Authority 1937-1969

By John L. Carey
Former Administrative Vice President
American Institute of Certified Public Accountants

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS
666 FIFTH AVENUE NEW YORK, N.Y. 10019

Copyright 1970 by the
American Institute of Certified Public Accountants, Inc.
666 Fifth Avenue, New York, N.Y. 10019

To

JOYCE

NOTICE TO READERS

The author is solely responsible for the contents of this book. In publishing it the American Institute of Certified Public Accountants accepts no responsibility for the accuracy of factual statements or for the validity of interpretive comment.

Table of Contents

Preface to Volume II .... *xv*

CHAPTER 1
The Drive for Better Financial Reporting 1

Montgomery's Farewell Address 3
Pressure for Better Financial Reporting 5
Challenges to the Practitioners 8
The Profession Responds 12
How Things Stood as War Struck 16

CHAPTER 2
A Crisis in Auditing 20

The McKesson & Robbins Case 22
The Institute Reacts 24
The New York Attorney General's Hearing 25
Informing the Membership 29
Implications for Legislation 32
Extensions of Auditing Procedure 33
The SEC Findings 35
The Ethics Committee Report 38

CHAPTER 3
War Years 42

Defense Preparations 43
Pearl Harbor 45
Accounting Manpower 46
Consulting Activities 48
Technical Activities 49

Keeping the Members Informed 50
The Institute's Organization 51
Aftermath 52
Management Services 54

CHAPTER 4
Pressure for Comparability of Earnings 56

Focus on Earnings Per Share 58
Pressure From the SEC 60
All-Inclusive vs. Earning-Capacity 65
Price-Level Accounting 68
Pressure From Academia 70
Pressure From Analysts 71
Pressure From the Press 72
Pressure From Within the Institute 73
Countervailing Pressure 80
The Committee on Accounting Procedure 84

CHAPTER 5
Time for a Change—The APB 90

A Fresh Start 92
The Investment Credit 98
Field Day for the Press 104
The SEC's Position 105
The SEC Under Questioning 108
The Council Acts 110
The Special Committee 117

CHAPTER 6
Increasing Authority of the APB 119

Observations From the SEC 122
A Proposal for an Accounting Court 124
Uniting on a Common Objective 127
Increased Pressure From the SEC 130

Industry Resistance 133
The Press Keeps Score 135
The APB's Achievements 139
The Seaview Symposium 142

CHAPTER 7
Evolving Audit Responsibility 145

The Concept of Auditing "Standards" 147
Procedural Guidelines 149
Certificates, Reports, Opinions 151
Influence of the SEC 155
Exceptions and Disclaimers 159
Codification of Auditing Standards and Procedures.... 162
Compliance 164
The Disciplinary Machinery Works 165
Influence of the Banks 168
The Practice Review Committee 169
Influence of the Courts 170
Protection Against Unjust Claims 173

CHAPTER 8
The Concept of Independence 175

The "Appearance" of Independence 176
Independence "in Fact" 179
The Council Speaks 181
Tighter Rules by SEC, Illinois, New York 182
Facing Up to the Issue 185
Independence and Management Services 191
Tentative Conclusions 199

CHAPTER 9
The Defense of Tax Practice 204

The National Organizations Disagree 206
Representation of Taxpayers 212

Local Action 214
Formation of National Conference 216
A Dash of Cold Water 217
The Bercu *Case* 219
The Drift Toward Conflict 221
The Conway *Case* 223
Mounting Concern 224
Appeals to the Federal Government 225
Another Blow 226
More Action on the Legislative Front 228
Resumption of the National Conference 229
A Statement of Principles 230
Hostilities Not Eliminated 233
Another Crisis in the Conference 237
A Change of Policy 238
The Agran *Case* 240
Appeal to the Treasury Department 241
Appeal to Congress 242
Appeal to the Public 243
Dean Griswold Acts 244
Another Effort at Peacemaking 245
The Treasury Acts 251
The National Conference Reconstituted 253
The Tax Court 255
Administrative Practice Legislation 255

CHAPTER 10
Education and Experience 258

Proposed Educational Standards 259
The Commission on Standards 264
The Bailey Committee Report 269
The Hansen Committee Report 272
The Ford and Carnegie Reports 273
Horizons for a Profession 276
Policy Changes 280

CHAPTER 11
Continuing Education and Recruiting 286

"Contemporary Accounting" 287
Focus on Staff Training 288
"The Million-Dollar Handbook" 289
The First Institute Courses 291
A Turning Point 294
The Professional Development Program 296
Attracting Competent Personnel 299
The Testing Program 300
Recruiting Activities 305

CHAPTER 12
CPA Requirements and Legal Regulation 311

Educational Requirements 312
The Joint Committee on Accounting Education 313
Experience Requirements 314
The CPA Examination 315
Legislative Problems 321
Regulatory Legislation 322
A New Approach 325
The National Society of Public Accountants 328
Changing Course Again 329
An Affirmative Policy 332
Negotiations With the National Society 334
Legislative Conferences 337
Higher Accreditation? 338

CHAPTER 13
Small Firms and Large Firms 339

Mergers 342
Change of Institute's Name 343
Legislative Restrictions 344
State Society Relations 345
Membership Relations 349

Advisory Committee of Local Practitioners 350
Large Firms Consulted 352
The Bankers' Influence 353
Future of the Local Practitioner 356
Membership Services 357
Library and Information Service 358
Publications 359
Continuing Education 361
Insurance Plans 361
Action in Washington 362
Practice Management 363
Management Services 363
The Computer Program 364
Evaluation of Audit Capacity 366
The Attitude of Large Firms 368
International Affairs 369

CHAPTER 14
Public Service and Public Relations 374

Early Public-Relations Efforts 375
A New Look 379
Later Public-Relations Efforts 380
Public Service 382
The Public Spotlight on Financial Reporting 384
"The Auditors Have Arrived" 386
Improving Communications 389
Public-Relations Policy and Program 391
The Profession's Attitude 393

CHAPTER 15
Toward a Viable Tax System 395

Extensions for Filing Returns 397
For a Non-Partisan Tax Commission 398
Tax Accounting and Business Accounting 400
Technical Tax Advice 404

Reorganization of the Bureau 405
Tax Legislation and Regulations 406
General Policy on Taxation 409
Other Activities in the Tax Area 412

CHAPTER 16
Improving Government Accounting 415

The Conference on Municipal Accounting 417
The Conference on Federal Government Accounting.. 420
The Federal Government Corporations 422
Origin of the Joint Program 426
Hoover Commission Proposals 428
A New Comptroller General 431
The Joint Financial Management Improvement Program 431
Management Audits 432
The Commission on Budget Concepts 433
The Federal Government Accountants Association 433
The Institute's Washington Office 435
Local Government Accounting 438

CHAPTER 17
Ethical Responsibilities 440

Widening Scope of Activity 443
Progress Toward Co-ordination 444
Ethics as an Examination Subject 446
Operating Problems 446
Publications 448
Overhauling the Rules 448
Technical Standards 449
Practice Review 455
Independence 456
Promotion, Publicity and Encroachment 460
Competitive Bidding 465
Practice in Corporate Form 468

Confidential Relationship 475
Contingent Fees 476
Related Occupations 476
Mixed Partnerships 477
Employment of Lawyers 478
Responsibilities in Tax Practice 479
Responsibilities in Management Services 482

CHAPTER 18
Planning for the Future 485

Identifying Long-Range Objectives 486
Status of Members Not in Practice 486
Relations With Other Organizations 488
Changes in Personnel 490
Successes and Defeats 491
"Where Is It Headed?" 492
A New Approach 493
Planning for the Profession 495
Planning for the Institute 497
Conclusion 503

APPENDIX A

Officers of the American Institute of Accountants and American Institute of Certified Public Accountants to 1969 505

APPENDIX B

Gold Medal Award Winners 514

Preface to Volume II

THE first 50 years of the accounting profession's existence in the United States, reported in the first volume of this history, might be described roughly as the period of organization, of foundation-building, of getting ready.

The following 32 years were packed with action, crisis, and achievement.

It has been much more difficult to write about the second period than the first—primarily because more happened in the later years. To keep this book to a manageable size, many interesting and important events have had to be left out—and those left in have not been described in as much depth as might be desirable. Almost every chapter could be expanded into a book—and I think it would be useful to do so. Perhaps this possibility would interest Ph.D. candidates.

What I have tried to do is to show trends—the cause-and-effect relationships, the reasons why things happened, the thinking behind them. This, I hope, may provide useful background for consideration of future problems.

To make the book readable has been a prime objective. It is not intended mainly as a reference work, but as a narrative of how the profession got where it is. The book needs to be read through to accomplish its purpose.

To encourage reading, countless details have been omitted. Dates and names have been mentioned sparingly—the latter only when personalities seemed to have some significant re-

lationship to the events described. This approach results in a gross injustice to thousands of men who contributed substantially to the decisions and actions covered in this volume. It is also regrettable that recognition could not be accorded to all of the past and present members of the Institute's staff who have made important—sometimes even brilliant—contributions to the profession's progress.

I am indebted to Elizabeth Arliss Nicholson for invaluable help in research and in preparing the manuscript, and also to the following men who were kind enough to comment on drafts of various chapters:

SAMUEL J. BROAD
CLIFFORD V. HEIMBUCHER
JOHN B. INGLIS
ALVIN R. JENNINGS
JOHN LAWLER
ELLSWORTH H. MORSE, JR.
LEONARD M. SAVOIE
J. S. SEIDMAN
FREDERIC H. SMITH
FRANK WEITZEL

None of these gentlemen, of course, has any responsibility for the final product.

The raw material for this volume came almost entirely from the official records, publications, and files of the American Institute of Certified Public Accountants, from public records such as SEC releases and Congressional committee hearings—and from my own observations.

For general background I relied on Samuel Eliot Morison's *The Oxford History of the American People,* Oxford University Press, New York, 1965.

JOHN L. CAREY

Salisbury, Connecticut
December 16, 1969

CHAPTER 1

The Drive for Better Financial Reporting

NINETEEN THIRTY-SEVEN was a jubilee year for the American Institute of Accountants. Its direct predecessor, the American Association of Public Accountants, had been founded in 1887. The fiftieth anniversary celebration held at the Waldorf-Astoria Hotel in New York was a brilliant affair.

For the first time in 15 years, the certified public accountants of the United States had completed a year under the banner of one national organization. The American Society of Certified Public Accountants had merged with the Institute the year before. Membership had spurted, activities had expanded, and prominent members of the Society had been brought into the Institute's official family. Relations with the state societies had been strengthened. Altogether the outlook was encouraging, and the mood of the 1,500 members in at-

tendance at the fiftieth anniversary meeting was one of optimism and goodwill.

However, the nation and the world were in a state of confusion and apprehension.

President Roosevelt's New Deal had been bitterly fought by the business community, whose members feared that the rapid extension of the federal government's power into economic and business affairs was leading toward socialism and dictatorship.

In truth, as Samuel Eliot Morison says, "The New Deal seemed newer than it really was, partly because progressive principles had largely been forgotten for 13 years, but mostly because the cards were dealt with such bewildering rapidity."[1] New laws were passed and new federal agencies were created with dazzling speed. It was difficult for businessmen—and accountants—to keep up with the new rules of the game.

Disillusionment with the capitalist system had been a reaction of many Americans to the hard years of the depression. In 1937 there were still some ten million unemployed, down less than three million from the high point of 1932. Discontent with the American system led to the formation of both fascist and communist groups in the United States. "Polarity being a weakness of intellectuals," says Morison, "many decided to save America by embracing one of the two competing ideologies in Europe—fascism and communism."

The American fascist movement made little progress, but communists infiltrated organizations of farmers, labor unions, and various political organizations which consciously or unconsciously served as fronts for policies that were dictated in Moscow.

Economically, socially, and politically the United States in 1937 was in some disarray. The uneasiness of the business community was reflected in the most important address at the Institute's fiftieth anniversary celebration, delivered by

[1] *The Oxford History of the American People,* Oxford University Press, New York, 1965.

Robert H. Montgomery, as retiring president of the Institute. His opening words were, "There is a war of ideas sweeping the world."

Montgomery's Farewell Adderss

This speech was the last one made by Colonel Montgomery as an officer of a professional accounting society. This remarkable man had first come to prominence at the International Congress of Accountants in 1904, 33 years previously. Together with George O. May—who, by coincidence, had also achieved professional visibility at the 1904 Congress—Colonel Montgomery had been in the vanguard of the profession throughout the intervening years. Mr. May was respected by most practitioners as the profession's philosopher, planner, and strategist, while Colonel Montgomery was widely regarded as the activist, the fighter, the leader of the rank and file.

In his valedictory statement in 1937, Colonel Montgomery, at the age of 64, after 45 years of professional activity, offered his candid view of where the profession stood and where it ought to go.

He said quite frankly that, while the accounting profession had advanced rapidly, most of its members were only partly trained: in spite of themselves, certified public accountants had been thrust into a position of vital importance in the community. But, he continued:

> . . . we cannot be sure that our relations with government, business and finance will remain static.
>
> Fifty years ago in the United States the public accountant was little known, little recognized, little wanted. His virtues were unheralded, unsung. He was little known because his kind were few and because enterprises were relatively small, and in most cases their accounts as well as their affairs were supervised by the owners. He was little recognized because the matters which were referred to

him at that time were relatively unimportant, and this unimportance tended to reduce him to the level of a clerk. . . .

Even when he was most needed it was feared that the employment of public accountants would be looked upon as evidence of suspected fraud or irregularity, losses and doubt regarding financial strength. Even when business grew bigger and public accountants were a little better known, there was a reluctance to call one in. As late as 30 to 40 years ago many investigations by public accountants were made secretly, often at night and on Sundays. . . .

We must admit that the steps in our ascent were not easy ones. When recognition is grudgingly accorded it is more vulnerable than when it is gladly acclaimed. We cannot compare the accountant with the doctor of divinity or the doctor of medicine. . . .

We are here today because there was and is a need for us. That demand will continue as long as people feel a need to know the truth, whether or not it hurts. . . .

Our profession always has had a vision—this urge to find and tell the truth—and we should cling to it and continue to strive for its accomplishment. I do not want to see our growth depend on anything else than that which has made us what we are today. We shall retain our strength just as long as we retain our independence—no longer.

Colonel Montgomery warned the profession not to assume virtues or abilities that it did not possess, which could lead to expectations that could not be realized: "We would like to be taken for what we are and no more."

In discussing the protection of investors, he said, "If accountants are to have any part in assisting . . . to avert another panic, I think it will have to take the form of some publicity of earnings per share. For example, would it not check unwise speculation if anyone buying stock selling at more than 20 times current earnings were required to pay for it in full?"

The address concluded with an appeal to the profession to *fight*: to fight to raise standards, to expel members guilty of unworthy conduct, to achieve a sane federal income-tax law, to preserve the prestige of the CPA certificate, to encourage sound business practices, to maintain the independence of accountants from private or governmental pressures, to pro-

mote clear financial statements and full disclosure, and finally, "Let's fight weasel words. Let's fight bunk whenever and wherever it appears."

He was strictly "on target" as the next few years would demonstrate.

Pressure for Better Financial Reporting

Prior to the stock-market crash of 1929, there were no authoritative standards governing corporate financial reports. As early as 1926, however, George O. May perceived the need for some rational conceptual foundation on which the responsibility of independent auditors could be based. He also saw that, lacking any statutory underpinning comparable to the English Companies Acts, the accounting profession would have difficulty in establishing authoritative ground rules which corporations would feel obliged to follow in their financial statements. By enlisting the co-operation of the New York Stock Exchange, which did have authority over listed companies, he and his associates on the Institute's committee on co-operation with stock exchanges were able to break new ground. They produced the famous pamphlet, "Audits of Corporate Accounts,"[2] published in 1934, which presented a logical and persuasive statement of the nature of corporate accounting, the responsibilities of independent auditors, and the manner in which safeguards might be established against the issuance of misleading financial statements.

This work was completed in the nick of time. The securities legislation of 1933 and 1934 invested the Securities and Exchange Commission with power to prescribe accounting methods to be followed by registrants in statements filed with

[2] The evolution of this document is described in detail in Volume I of this work.

the Commission. It also left to the Commission discretion to determine whether or not financial statements of registrants should be audited by independent accountants.

The Commission's decision not to prescribe uniform accounting rules, and to require independent audits, was due at least partly to the fact that the Institute and the Stock Exchange had already made a long step forward. No doubt the Commission was also impressed with the difficulty of prescribing uniform principles of accounting, and of satisfying itself as to the reliability of financial statements of registrants without the aid of independent auditors.

In any event, the SEC decided to give the accountants a chance to show what they could do, and to move forward cautiously without radical innovations in accounting for the time being.

The rationale for financial reporting approved by the Institute and the New York Stock Exchange was essentially simple. Its major elements were as follows:

1. Principles of accounting cannot be arrived at by pure reasoning, but must find their justification in practical utility.
2. Prescription of a detailed set of rules binding on all corporations of a given class would be retrogressive.
3. Corporations should be permitted to choose their own accounting methods within reasonable limits, but should be required to disclose such methods and apply them consistently from year to year.
4. A relatively small number of broad principles of accounting should be adopted as a framework within which the validity of specific applications could be tested.

One important part of this rationale fell by the wayside: in implementing the program, the Exchange did not require disclosure of the specific accounting principles followed by individual corporations in their financial statements.

The standard form of auditor's report approved by the Institute and the Exchange included a representation that the

financial statements fairly presented position and results "in accordance with accepted principles of accounting consistently maintained by the company during the year under review."

Yet there existed no comprehensive statement of accepted accounting principles. Since disclosure of the accounting principles or methods followed by individual companies was not required, the phrase "accepted principles of accounting" became shrouded in ambiguity. What were they? Where could they be found? In these questions lay the seeds of future discontent.

However, consistency in the application of accounting principles and methods was required, and it was widely assumed that this was more important than the particular principle or method which might be selected. This assumption was sound enough from the viewpoint of an individual investor in a single company, since it would permit valid comparisons of the net income of one year with that of another, but it ignored the growing desire for a basis of comparison of the profits of one corporation with those of another.

An indirect reference to this problem appears in the first Accounting Research Bulletin issued by the Institute's committee on accounting procedure:

> It is of interest to point out that "uniformity" has usually connoted a similar treatment of the same item occurring in many cases, in which sense it runs the risk of concealing important differences between the cases. Another sense of the word would require that different authorities, working independently on the same case, should reach the same conclusion. This at any rate is an ideal which all will agree to strive for, and perhaps is more readily attainable.

As it turned out, all did not strive for this ideal with sufficient urgency to satisfy the demands of the rapidly growing investing public, with results which will be described in later chapters.

At any rate, in the absence of a comprehensive code of accounting principles, the SEC acquiesced in the "common-law" approach to the problem by ruling on specific accounting ques-

tions as they arose. The chief accountant of the SEC would often seek the advice of the Institute's committee on co-operation with the SEC, or the advice of individual accountants believed to be familiar with the subject matter under consideration, before deciding whether the accounting treatment of a specific transaction in a given case was appropriate or not.

In January 1937, the chief accountant, Carman G. Blough, issued the first release on a specific accounting question—treatment of federal income and excess-profits taxes and surtax on undistributed profits. A few months later the Commission inaugurated the series of official opinions by the chief accountant, which were announced to be designed "for the purpose of contributing to the development of uniform standards and practice in major accounting questions." Accounting Series Release No. 1 dealt with the treatment of losses resulting from revaluation of assets. These releases took on the authority of rules, and the initiative was slipping from the profession's hands.

Challenges to the Practitioners

Just about a year earlier, the reorganized American Accounting Association, dominated by the academic branch of the accounting community, had flung down a challenge to the practicing profession. In a new statement of objectives, the Association said, "After a quarter century and more of active discussion and experimentation in this country, many of the simplest and most fundamental problems of accounting remain without an accepted solution. There is still no authoritative statement of essential principles available on which accounting records and statements may be based. Public accountants . . . have been asked to certify to the correctness and adequacy of accounting statements, when no satisfactory criteria of correctness and adequacy have been agreed to."

Shortly thereafter the Association's executive committee pub-

lished a "Tentative Statement of Accounting Principles Affecting Corporate Reports," which contained this statement:" Every corporate report should be based on accounting principles which are sufficiently uniform and well understood to justify the forming of opinions as to the condition and progress of the business enterprise behind it." The document as a whole was relatively brief. Couched in broad, general terms, it focused on what were considered to be three major aspects of corporate accounting—cost and values, measurement of income, and capital and surplus.

The issuance of this statement irritated many practitioners of accounting. It appeared to be a step toward establishment of a uniform code of accounting principles—a concept formally rejected by the Institute, which was co-operating with the SEC in the "common-law" approach of settling each case on its merits in view of the surrounding circumstances.

In one of his earliest addresses as chief accountant, Carman Blough told the Ohio Society of Certified Public Accountants about cases involving questions of accounting principle on which the Commission had to rule. He mentioned 19 instances in which stop orders had been issued because of unacceptable accounting practices. As illustrations he cited eight cases of improper accounting or inadequate disclosure on which the Commission had been required to take action. In conclusion he said:

> The Securities and Exchange Commission is anxious to develop accounting practice and procedures on a high level, to bring to the investor for whose protection it was created a more dependable body of information than he has ever had before. To do so will require the support of the accounting profession. The accountants and the Commission working at cross purposes will accomplish little, and in my opinion the cause of accountancy will suffer. On the other hand, if the accountants and the Commission co-operate, they can do much toward correcting undesirable accounting practices.

Later Mr. Blough spoke more bluntly at a meeting of the New York State Society of Certified Public Accountants.

He reminded the audience that the SEC had chosen not to use its power to prescribe definite rules and regulations on accounting. Instead, it had chosen to review individual financial statements filed with it, to determine whether the methods followed in their preparation were generally recognized, and if not, to cause them to be amended in accordance with generally accepted principles. This policy, he pointed out, placed a large measure of responsibility on the certifying accountant for the way in which financial statements were presented. The Commission required that the certifying accountant must state his opinion with regard to the financial statements and the accounting principles and procedures followed by the registrant. The precedent for this requirement, Mr. Blough said, was found in the form of an accountant's report developed in the correspondence between the Institute and the New York Stock Exchange.

However, Mr. Blough continued:

> Because of the lack of agreement among accountants with respect to important accounting principles, it has been difficult to determine what position should be taken with respect to many of the statements filed with the Commission in which such controversial questions have been involved. . . . In numerous instances where we believed the method of accounting to be improper, we have accepted complete revelation of significant matters instead of insisting upon a revision of accounting statements as we would have if there had been a violation of an unquestionably accepted accounting principle. . . . Often, the principles with respect to which there is marked difference of opinion among accountants are such that in order to make the statements not misleading, it is necessary that voluminous notes be attached thereto. . . . Certainly the Commission would prefer that financial statements be so prepared as to eliminate the necessity for extensive footnotes. . . .
>
> The term "generally accepted accounting principles" has been widely used in accounting literature, particularly by the American Institute of Accountants and the Securities and Exchange Commission; yet I do not know of any satisfactory definition of the term. . . . Almost daily, principles that for years I had thought were definitely accepted among the members of the profession are violated in a registration statement prepared by some accountant in whom I

have high confidence. Indeed, an examination of hundreds of statements filed with our Commission almost leads one to the conclusion that aside from the simple rules of double-entry bookkeeping, there are very few principles of accounting upon which the accountants of this country are in agreement. . . . I have been forced to the conclusion that procedures so generally followed among accountants as to constitute substantial precedent are not always fundamentally sound.

To drive home his point, Mr. Blough cited some 30 examples of accounting treatments which had caused the Commission concern, but which reputable accountants considered proper. In the course of these illustrations, he said:

It has been quite amazing to see the number of occasions that accountants have found for writing off against capital surplus items that, according to my standards, can properly be handled only through the income account or directly against earned surplus. . . . The desirability of using surplus arising through appreciation to write off operating deficits, though there seem to be many who support that practice, appears to me to be very questionable, and the use of surplus created by the appreciation of one class of assets to revalue other assets downward is to me untenable.

In concluding his long list of questionable accounting practices, Mr. Blough said:

In each of the examples mentioned some accountant has supported each conflicting viewpoint and has averred in his certificate that the statements reflected the application of accepted accounting principles. . . .

What the future policy of the Commission will have to be I am not prepared to say, but we are reluctant to undertake the prescription of principles to be followed except as a last resort. It is hoped the profession will itself develop greater consistency in the many places where uniformity appears essential. . . .

The cumulative effect of this speech was devastating. Mr. Blough's challenge, in conjunction with the earlier challenge of the American Accounting Association, made it clear that if the

Institute wished to maintain a position of leadership it would have to do more than it had so far done to promulgate authoritative accounting principles.

The Profession Responds

One of the accountants who was deeply concerned about the profession's posture was Warren W. Nissley—that same energetic partner of Arthur Young & Company who ten years before had conceived and brought into being the Institute's bureau for placements (see Volume I of this work). Thomas G. Higgins, one of Nissley's partners, later wrote, "When Warren Nissley was on a crusade, his tenacity was terrific. We in the New York office had accounting principles morning, noon, and night. . . . This aggressiveness of Warren's paid off however; the profession took heed. It was to a great extent due to Warren's crusade that, at the American Institute's Council meeting in September 1938, the committee on accounting procedure recommended an increase in its own size and the establishment of a research division, with paid assistants, with a view toward eventually formulating pronouncements on specific procedures and practices."

Mr. Nissley undoubtedly discussed his concern with George O. May, who was then chairman of the Institute's eight-man committee on accounting procedure. The committee was operating without the assistance of technical staff and had offered no specific recommendations on accounting principles for several years.

In the fall of 1938, this committee reported to the Council, "The committee on accounting procedure, recognizing the existence of a widespread demand for greater uniformity in accounting, has given continuous consideration to the question how progress in the desired direction could most wisely be made."

After discussing possible alternatives the report continued,

"Another more ambitious suggestion is that the Institute should create, under the control of a somewhat enlarged committee on accounting procedure, a research department for the purpose of preparing studies on particular questions, distributing them in such a way as the committee might deem expedient, and ultimately formulating rules on specific points which would be binding on the members of the Institute unless and until adverse action upon them should be taken, either by the Council of the Institute or the membership at large."

This proposal met with favor and the Council authorized action along the lines suggested. In May 1939, the committee reported remarkable progress. It had been enlarged to 22 members. The president of the Institute, Clem W. Collins, had been designated as chairman in order to emphasize the committee's authority and prestige. George O. May was vice-chairman and the active operating head. The committee included representatives of many local accounting firms as well as partners of larger firms, among whom was Warren W. Nissley. Its membership also included Carman Blough of the SEC, and three outstanding academicians, Roy B. Kester of Columbia University, A. C. Littleton of the University of Illinois, and William A. Paton of the University of Michigan.

Thomas H. Sanders, professor of accounting at the Harvard Graduate School of Business Administration, had been retained as research director, with the understanding that he would devote approximately half of his time to this work.

Professor Sanders was one of the authors of a study published in 1938, under the sponsorship of the Haskins & Sells Foundation, entitled "A Statement of Accounting Principles." His collaborators were Professor Henry Rand Hatfield and Underhill Moore, a lawyer. According to Reed Storey,[8] "the authors apparently interpreted their mission as one of reporting on the weight of opinion and authority. At least their emphasis was on codification of accounting practice rather than on re-

[8] In *The Search for Accounting Principles,* American Institute of Certified Public Accountants, New York, 1964.

examination of individual practices. The result was largely uncritical acceptance of existing methods. The committee took the position that it was the duty of management to decide what information should be given in the financial statements and how it was to be shown. The role of the accountant was restricted to indicating whether appropriate disclosure had been made."

Professor Sanders was not immediately available when the committee on accounting procedure was reorganized, and Professor W. Arnold Hosmer of Harvard served as acting director, pending the return of Professor Sanders from abroad. Richard S. Claire, who had had both teaching and public accounting experience, had been engaged on a full-time basis as assistant to the director.

By September 1939 the committee was able to report with pride the issuance of three Accounting Research Bulletins.

ARB No. 1 consisted of a general introduction outlining the committee's approach to the new program and restating rules formerly adopted by the membership, the Council, or the committee on accounting procedure. An excerpt from its comment on uniformity is quoted on page 7 of this chapter. In addition, in the general introduction it was said that accounting problems had come to be considered more from the standpoint of the current buyer or seller in the market of an interest in an enterprise than from the standpoint of a continuing owner; as a result there had been a demand for a larger degree of uniformity in accounting, "although it may be pointed out that the change of emphasis itself is bound to lead to the adoption of new accounting procedures, so that for a time diversity of practice is likely to be increased as new practices are adopted before old ones have become completely discarded." Increased recognition of the significance of the income statement was also cited as a result of the changing approach to corporate accounting.

The committee's rules, as explained in ARB No. 1, provided that pronouncements were to be adopted by a two-thirds vote of its members. Dissents would be published. Pronouncements

were not to be retroactive, nor applicable to immaterial items. Exceptions to the pronouncements might be permissible in specific cases, but the burden of proof for justification of departures would rest upon those who adopted other treatment.

It was emphasized that the accounts of a company were primarily the responsibility of its officers: the responsibility of the auditor was to express his opinion as to the correctness of the accounts, and to make qualifications to the extent that he considered necessary to explain, to amplify, to disagree, or to disapprove.

Accounting Research Bulletins Nos. 2 and 3 dealt with two areas in which current practice had been subject to criticism—unamortized discount and redemption premium on bonds refunded, and quasi-reorganization or corporate readjustment.

Between September 1939 and September 1941, nine additional Accounting Research Bulletins were published. Three of these were special bulletins dealing with accounting terminology. The others dealt with foreign operations and foreign exchange, depreciation on appreciation, comparative statements, combined statement of income and earned surplus, real and personal property taxes, and corporate accounting for ordinary stock dividends.

There was no reference to the original idea that the conclusions of the committee would be "binding on the members of the Institute unless or until adverse action upon them should be taken either by the Council of the Institute or the membership at large." Instead, all these bulletins contained at the end a standard note to the effect that they represented the considered opinion of at least two-thirds of the members of the committee on accounting procedure, but that, except in cases where formal adoption by the Institute had been secured, the authority of the bulletins rested upon the general acceptability of the opinions so reached. The note also stated that while it was recognized that any general rules might be subject to exception, it was felt that the burden of justifying departures must be assumed by those who adopted other treatment.

Despite the permissive approach, the impact of this new

program was immediate and salutary. It was regarded as a constructive response to the criticisms of the Securities and Exchange Commission and the challenge of the American Accounting Association. The Accounting Research Bulletins soon had a visible influence on corporate accounting. While they did not establish uniform practices, they did gradually narrow the areas of difference by indicating preferred treatments among alternatives which up to then had had support in precedent. The Securities and Exchange Commission added authority to the findings of the committee on accounting procedure by insisting generally that registrants follow the recommended practices.

Another influential treatise emerged from the academic community in 1940, a monograph entitled *An Introduction to Corporate Accounting Standards,* by Professors W. A. Paton and A. C. Littleton, published by the American Accounting Association. This was in effect an elaboration and expansion of the basic concepts on which the Association's "Tentative Statement of Accounting Principles" was based. This monograph gained wide acceptance for the proposition that the matching of costs and revenues was the appropriate basis for income measurement, rather than the process of asset and liability valuation.

How Things Stood as War Struck

When the Japanese bombed Pearl Harbor on December 7, 1941, the country went on an all-out war footing, and the committee on accounting procedure was forced to devote itself almost exclusively to questions involving war transactions.

Dr. Sanders resigned as director of research in order to undertake duties related to the defense program in Washington. For a short time Professor James L. Dohr of Columbia University held this post, but he, too, soon found it necessary to resign. Dick Claire left also to participate in the war effort.

George M. Farrand, who had been engaged as research assistant to succeed Mr. Claire, carried on the work of the research department.

Carman Blough had left the Securities and Exchange Commission to become a partner of Arthur Andersen & Co. Later he resigned from that firm to assume a position in the government related to the war effort. William W. Werntz, former professor of accounting at the Yale Law School, had become chief accountant of the SEC.

In June 1941, the American Accounting Association completed and published its second statement on accounting principles, entitled "Accounting Principles Underlying Corporate Financial Statements." The word "Tentative" was omitted.

The similarities and differences between the Institute's approach to the problem and that of the Association are clearly set forth in *The Search for Accounting Principles,* written by Reed K. Storey in his capacity as the Institute's director of accounting research, and published by the Institute in 1964:

> Three basic similarities in the programs of the two associations stand out: (1) the two societies had exactly the same objective, i.e., the improvement of financial accounting and reporting practice by reducing the number of acceptable alternative procedures, (2) both saw financial accounting as essentially a process of cost and revenue allocation rather than as a process of asset and liability valuation, and (3) both looked upon accounting principles as being derived from accounting practice. . . .
>
> Yet in spite of the fact that there was substantial agreement on basic matters . . . important differences developed. Basic agreement involving the goal to be achieved did not result in agreement regarding the method of reaching it. Acceptance of matching as the basis of income determination did not result in a single theory for its application. Joint recognition that accounting principles were to be derived from practice did not result in agreement as to what the term "principles" meant or who was to be responsible for their derivation.

Dr. Storey went on to say that the Association believed that improvement could best be achieved by strengthening the overall framework which supported accounting practice—that

is, by formulating interrelated, consistent, and comprehensive principles of accounting. In contrast the Institute adopted what was called the "piecemeal" approach to accounting principles, designed to give immediate help to the practicing accountant faced with a special problem. The committee on accounting procedure accordingly considered specific topics as the need arose, and, if possible, recommended one or more alternative treatments as definitely superior to other procedures formerly regarded as acceptable.

"The different approaches of the two professional societies," wrote Dr. Storey, "in fact complemented each other. The ultimate conclusions were surprisingly alike."

While a "statutory" body of accounting principles accepted by all concerned was still lacking, accounting practices had in fact improved over what they had been ten years earlier, and a pattern of accounting development for the next 25 years was being established.

Corporate managements and practicing accountants—not to mention students who would become managers or auditors—could not fail to be influenced by the proliferating literature and pronouncements on accounting principles.

The SEC steadily exercised its power to enforce compliance with preferred practices. Prior to the entry of the United States into World War II, the Commission had issued 20 Accounting Series Releases. But in a far greater number of cases it had required correction of unacceptable accounting procedures through deficiency letters, stop orders, or informal consultations with registrants.

At the end of the Institute's fiscal year in the fall of 1941, Mr. May retired as vice-chairman—to all intents and purposes, chairman—of the committee on accounting procedure, although he remained a member of the committee for several more years. He had attained the age of 66. For more than 40 years, in many capacities, he had labored enthusiastically on behalf of the profession. For the past 15 years, freed of administrative responsibilities in his own firm, he had devoted a

major part of his time to the development of a philosophy on which independent auditors could justify their function, and to the articulation of concepts and principles against which their performance could be measured. His contribution to the improvement of corporate financial reporting in the United States was outstanding.

The chairmanship of the committee on accounting procedure was assumed in 1942 by Walter A. Staub, partner of Lybrand, Ross Bros. & Montgomery—that same Walter Staub who had exhorted a stubborn Council in 1934 to work toward a merger of the American Society with the Institute (see Volume I of this history).

Progress was being made in avoiding a crisis over accounting principles. But meanwhile another crisis had developed in the area of auditing—the McKesson & Robbins case.

CHAPTER 2

A Crisis in Auditing

AT THE end of their first 50 years of existence as an organized profession, the practicing public accountants had done a far better job in establishing guidelines for independent audits than in delineating acceptable accounting principles.

The Federal Reserve Bulletin of 1917, "Approved Methods for the Preparation of Balance Sheet Statements," prepared by the Institute, was the first authoritative outline of what an audit should cover. The Institute's revision of this bulletin in 1929, entitled "Verification of Financial Statements," issued with Federal Reserve Board approval, recognized that changed conditions in the previous 11 years required some elaboration of the recommended audit procedures. This proved to be most fortunate, inasmuch as the negotiations with the New York Stock Exchange, leading to publication of "Audits of Corporate Accounts" in 1934, were facilitated by the knowledge that the profession had set its own standards for the conduct of independent audits.

A third revision of the bulletin was published by the Institute

in 1936, under the title "Examination of Financial Statements by Independent Public Accountants." This edition included new material, dealing with the significance and limitations of financial statements, and with the broad responsibilities of auditors, emphasizing the propriety of reliance on effective systems of internal control. This new material closely paralleled portions of the correspondence with the Stock Exchange. It established a conceptual foundation for auditing which had theretofore been lacking.[1]

The sequence of events showed foresight and intelligent concern for the public interest, as well as the interests of the profession itself.

Without these public declarations of the profession's concept of its own responsibility, and what it believed to be appropriate auditing procedures, it is also highly likely, in the light of the events shortly to be described, that the Securities and Exchange Commission would have felt obliged to lay down explicit rules governing the conduct of independent audits.

Even as it was, the 1936 bulletin reflected compromises on two moot points. Over the years there had been debate within the profession about the auditor's responsibility for inventories and receivables. Some members urged that auditors should examine physical inventories, although the traditional practice had been to rely on the accounting records. Others took the position, however, that since auditors were not appraisers, and therefore could not take responsibility for the valuation of inventories, it would be misleading to represent that they had physically inspected inventories, which might convey the impression that they accepted responsibility for their value.

With regard to accounts receivable, some members advocated direct confirmation with debtors, while others considered this step unnecessary when adequate systems of internal check and control existed.

As a result of these differences of opinion, the 1936 bulletin

[1] These developments are described in greater detail in Volume I of this work.

took a somewhat equivocal position on both points. Regarding inventories the bulletin said:

> The duties and responsibilities of the accountant in the case of quantities, quality and condition of stock vary with the circumstances, but he must rely principally for information as to quantities, quality and condition upon the responsible officers and employees of the company. . . .
>
> [Further, the accountant is obliged to:]
>
> Make reasonable inquiries and tests to ascertain that quantities have been carefully determined and that quality and condition have received due consideration. . . .
>
> Make a test comparison of the inventories with the stock records, if these are maintained, in support of quantities, prices, and values. Any material discrepancy should be satisfactorily explained.

With regard to accounts receivable, the bulletin said in part:

> The best verification of accounts receivable is to communicate directly with the debtor regarding the existence of the debt, and this course may be taken after arrangement with the client. While such confirmation is frequently considered unnecessary in the case of companies having an adequate system of internal check, it is one of the most effective means of disclosing irregularities.

The differences of opinion on these points were soon to be resolved, however, by the pressure of public opinion.

The McKesson & Robbins Case

On December 5, 1938, a complaint was filed in the United States District Court at Hartford, Connecticut, seeking the appointment of a receiver for McKesson & Robbins, a large, widely known and respected company engaged principally in the drug and chemical business. The complaint alleged that the company's officers and directors had fraudulently represented its assets as including inventories and accounts receivable which

did not exist. The court immediately appointed temporary receivers for the corporation.

After a frantic night of consultation, the New York Stock Exchange held up trading in McKesson securities at the opening of the market Tuesday morning, December 6. At 11:30 A.M. the Exchange's Board of Governors met and voted an indefinite suspension.

Financial statements of the corporation and its subsidiaries for the year ended December 31, 1937, certified by Price Waterhouse & Co., reported total consolidated assets in excess of $87 million, of which approximately $19 million were later found to have been fictitious—$10 million of inventory and $9 million of accounts receivable.

Newspapers throughout the country displayed banner headlines announcing these horrendous facts. As more information reached the public, the sensational character of the case provided materials for a stream of almost daily news reports and editorial comments.

It was revealed that the president of McKesson & Robbins, who had assumed the name of Coster, was in reality Philip N. Musica, who had previously been convicted of commercial frauds; that other principal officials of McKesson, also acting under assumed names, were in reality Musica's brothers; and that the group had contrived an ingenious scheme of falsifying financial records and supporting documentation, which had completely deceived the auditors. All this added up to a juicy piece of scandal.

The details of the case were published in full in 1940 in the *Report on Investigation of the Securities and Exchange Commission in the Matter of McKesson & Robbins, Inc.* It became clear that an elaborate set of documents and records had been forged—purchase invoices, purchase orders, receiving tickets, shipping notices, bills of lading, debit and credit advices, statements from bankers, credit reports, confirmations from outside suppliers, inventory tally sheets, inventory summaries, and permanent records, constituting an apparently regular and orderly set of bookkeeping records.

The Institute Reacts

For the first two weeks after the news broke in December 1938, it was difficult for the Institute to obtain enough reliable information about the case to make any statement or take any action. Newspaper reports were fragmentary, and no official investigation had been completed.

However, under date of December 23, the Attorney General of the State of New York called a meeting of representatives of the accounting profession on January 6, 1939, to discuss questions related to the preparation of financial statements of large corporations. His letter did not reach the Institute's offices until December 27, following the Christmas holidays, but the invitation to send representatives to the meeting was immediately accepted—as indeed it had to be.

On December 28, a special meeting of the Institute's executive committee was held, after which a brief statement was issued to the press, to the effect that the Institute would carefully review customary auditing procedure in the light of the McKesson & Robbins case, but that available information indicated collusive action of company officers in forging a set of documents and records similar to those on which an auditor was entitled to rely. The executive committee's statement referred to customary auditing procedure set forth in the bulletin, *Examination of Financial Statements by Independent Public Accountants,* and said that auditing procedures had evolved over the years, and that the Institute would determine what, if any, changes in procedure should be adopted in the light of the current revelations. The statement concluded: "The auditor's problem always is to find means of affording adequate protection at a cost which will not constitute an undue burden on the great majority of corporations which are honestly administered. Out of the present discussion may evolve plans for closer co-operation between accountants and directors."

This statement was widely published in the press, sometimes with comment and sometimes without.

Business Week suggested that the result would be "divorcement of the employer-employee relationship that now exists between corporation management and independent auditors."

The *Hartford Times* said: "There is, readily enough, a loophole for dishonesty in the practice whereby management orders and defines the scope of the work to be performed by outside auditors, which could be closed if directors, as those directly responsible to the stockholders, took over the function."

Ralph Hendershot, in the *New York World Telegram,* said that the Institute's statement was hardly satisfactory if the certified public accountants were to receive the full support and confidence of the general public. He said, in part, "Few professions have been 'sold' to the public more thoroughly than have accountants."

On December 29, 1938, the day after the executive committee meeting, the Securities and Exchange Commission ordered an investigation of the McKesson case, focusing on the extent to which prevailing auditing standards and procedures were adhered to by the independent auditors of McKesson, and the adequacy of the safeguards inhering in such standards and procedures to assure reliability and accuracy of financial statements.

The entire accounting profession was, in effect, on trial.

The New York Attorney General's Hearing

At the meeting called by the New York State Attorney General, January 6, a joint statement was presented on behalf of the Institute and the New York State Society of Certified Public Accountants which said in part:

> The attitude of the professional accountancy bodies is quite clear. They invite and welcome, as they have always done, suggestions from any and all sources looking to improvement of auditing and accounting procedures. They have endeavored for many years, as

will be shown, to improve and refine the technique of auditing and to formulate sound rules of accounting as a basis for the presentation of financial statements.

There followed a description of the several editions of the Federal Reserve Board Bulletin, with the comment that for more than 20 years there had existed a written outline of audit procedures which had been generally accepted by the profession as standard practice. Reference was also made to the correspondence with the New York Stock Exchange, in which auditors' responsibilities were discussed and a standard form of auditor's report had been agreed upon.

Reference was also made to a resolution of the New York State Society of November 1938—just a month before the McKesson case had broken—with respect to the CPA's responsibility for inventories. This resolution stated that the certified public accountant was not qualified as a general appraiser or fitted to assume in all cases full responsibility for physical quantities, description, quality, condition, marketability, and valuation of inventory. The resolution concluded that an unqualified certificate by a CPA implied that he had exercised due care in his examination by making accounting tests and checks of the client's books of account and other available records pertaining to merchandise inventories; that he had received all information and explanations required from officers and employees responsible for the taking and valuation of the inventories—and so far as accounting methods permitted, had satisfied himself as to their substantial correctness; but as to ownership, physical quantities, description, quality, condition, marketability and valuation he had relied upon the representations of the management subject to such checks as had been obtainable from the records.

This was a strong and clear endorsement of the traditional viewpoint on the question.

The joint statement presented to the Attorney General by the Institute and the New York State Society went on to discuss the heavy responsibilities imposed upon auditors by professional standards, statutes, and court decisions, and the fact that

the financial statements were primarily the representations of the management. It was also pointed out that accounting was not a matter of mathematical accuracy, but largely a matter of judgment and opinion.

It was asserted that, in the absence of collusive fraud, the procedures outlined in "Examination of Financial Statements by Independent Public Accountants" would almost always disclose any important irregularities. Auditing procedures which could be presumed with any certainty to detect collusive fraud would have to be much more extensive and much more costly. However, it was conceded that there could be improvement in present practices and that the professional societies would consider such improvements in light of the current case.

It was suggested that auditors should be elected by stockholders rather than be appointed by the management (which had been the case in the McKesson situation). The English practice was cited. It was also suggested that auditors be invited to attend meetings of boards of directors and discuss with them any accounting questions which might arise, and that auditors should be informed of any questions in the mind of any director regarding activities of officers or employees of the company.

In conclusion the joint statement said: "As further facts are developed by the inquiries at present under way, various matters relating to auditing procedures involved will continue to receive our active consideration, with a view to recommending such steps as seem justified. In the meantime, we shall gladly endeavor to respond to questions relating to current auditing and accounting practice, and will welcome suggestions from the Attorney General or from others as to ways in which these practices may be improved."

The report of the Attorney General's office on the January 6 meeting, however, stated that while the conference had cleared the air of considerable confusion:

> It has definitely been shown that the balance sheet examination as conducted with the consent, approval and even direction of the

> American Institute of Accountants and by the New York State Society of Certified Public Accountants was not designed to disclose collusive manipulations by employees....
>
> Of course, the layman, not knowing this, properly has assumed that the form of examination was designed to disclose collusive fraud, and it has always given due credence to financial statements prepared by certified public accountants.

The Attorney General's report conceded that this limitation inherent in independent audits was completely disclosed years before through the publication of the correspondence between the Institute and the New York Stock Exchange. However, the Attorney General expressed the view that no publicity of this type would reach the investing public: "That group will always believe that, if a certified public accountant's name appears on the face of a balance sheet, such accountant has made sufficient examination to assure himself that the statement truly reflects the financial condition of the company. . . It is also our opinion that nothing short of clear unequivocal language on the face of the balance sheet showing what the accountant has not done will relieve the accountant of his moral, if not legal, responsibility in this regard. . . We believe rather that the balance sheet should contain the statement, 'inventory has not been verified' or 'accounts receivable were not tested or verified by direct communication.' "

Following a discussion of the practicability of verifying inventories and receivables—and the Attorney General was not willing to concede that this would be impracticable—the report continued: "The discussion disclosed that accountants were often limited by their clients as to expense and to the scope of the audit itself. When the accountant permits himself to be thus guided, he is lowering himself to the level of an employee and is forsaking his true duty to the public and others who rely on his report. If the profession will permit such domination, it is definitely relinquishing the very reasons for its existence."

The report contained several specific suggestions: (1) that the staff which conducts an audit be rotated periodically and that the audit program be varied each year; (2) too much

responsibility should not be delegated to staff assistants, and the responsibilities of partners should be clearly described; (3) only accountants qualified by state board examinations should be permitted to practice as public accountants.

The report concluded: "There is no intent in this report by us to lessen the importance of accountancy. On the contrary, we realize its need by businessmen more clearly than do most others. We know that it can serve a function to our economic life such as no other profession can or does. It has the power to lift the commercial enterprises of the nation to a high ethical level. In that respect, while criticizing its conduct in the past, we offer our praise for what the accounting profession has already accomplished, and we look forward to the improvements that it should and no doubt will make in its procedure and conduct."

Informing the Membership

The Attorney General's report, as well as the joint statement of the Institute and the New York State Society, were published in *The Certified Public Accountant* for the information of the membership.

Meanwhile, the SEC investigation was proceeding in New York under the principal direction of William W. Werntz, the Commission's chief accountant, with the assistance of legal counsel. Prominent members of the accounting profession were called upon to testify for the record as to the appropriate audit steps to be taken in situations comparable to the case under investigation.

All these proceedings received continuous and prominent publicity in the press.

The Institute's officers and committees were, meanwhile, hard at work. A special committee on auditing procedure, headed by Patrick W. R. Glover, senior partner of Barrow, Wade, Guthrie & Company, and including representatives of

a cross section of large and medium-sized firms, was analyzing the facts as they were disclosed and meeting day and night to consider what recommendations should be made.

While the Institute was responding to inquiries from public authorities and the press, it was also undergoing a barrage of questions and criticisms from its own members. How had the profession gotten in this mess? What would the Institute do about it? How could a prominent firm have failed to discover such egregious errors in the McKesson accounts? Was there going to be a whitewash? The unaccustomed exposure to the pitiless glare of critical publicity had brought some CPAs to a high emotional pitch.

In an effort to respond, the secretary of the Institute discussed the case at a meeting of the Pittsburgh Chapter of the Pennsylvania Institute of Certified Public Accountants on January 27, 1939—not quite two months after the case had hit the press. Excerpts from this talk were published in *The Certified Public Accountant* for the information of all members, including the following:

> For more than a month there has not been a day in which newspapers and financial and business magazines have not devoted attention to some aspect of accounting. . . .
>
> The present case . . . is the first one which, because of the magnitude of the sums involved and the extraordinarily dramatic circumstances, has captured the headlines and the editorial pages in all parts of the country.
>
> This case is distinguished from all others by the publicity which it has attracted . . . and the public reaction has surprised many accountants. We find that the public has believed that the certified public accountant was an infallible superman; that the signature of a CPA invariably meant that everything was perfect; that it was unnecessary to read the accountant's certificate or the financial statements to which it was appended as long as the three magic letters were in evidence. . . .
>
> Whether through its own fault or not, the accountancy profession seems to have been oversold. Its limitations have been overlooked, while its abilities have been emphasized. Now the public has been somewhat shocked to find that even auditors can be fooled by clever criminals. . . .

Never before has the public been particularly anxious to find out about accounting and accountants. . . . At a time like this public support can be found for every constructive proposal, whereas in the past there has been widespread apathy toward the problems of the young profession of accountancy. . . .

[The] statement by the executive committee was criticized by some members on the ground that it was a defense of the particular members of the Institute concerned in this case. These critics read something into the statement which is not there. Every line of it is the truth, and in the long run no group and no individual will suffer by stating the truth frankly, even though some people don't want to hear it.

The accountancy profession . . . has the best opportunity in its history to bring about changes which it may desire with the full support of clients, of the government, and of the public.

The February 1939 issue of *The Journal of Accountancy* contained extensive editorial comment on the McKesson case.

"Like a torrent of cold water," said the lead item, "the wave of publicity raised by the McKesson & Robbins case has shocked the accountancy profession into breathlessness. Accustomed to relative obscurity in the public prints, accountants have been startled to find their procedures, their principles, and their professional standards the subject of sensational and generally unsympathetic headlines."

Referring to the SEC investigation, which had already been in process for more than a month, the editorial said, "On an occasion of this kind accountants may congratulate themselves on the existence of the SEC. The presence of a body which possesses the authority, the facilities, and the informed personnel necessary to institute a thorough public inquiry is a fortunate thing for the profession, as well as business management and the investing public. Nothing will do so much to dispel vague rumor and shadowy suspicion as a statement of the facts by a governmental agency so well informed on accounting practices as the SEC. . . .

"The importance of independent audits and of accounting procedure will not be forgotten. If this incident reveals weaknesses in customary auditing procedure, those weaknesses can

be corrected. We predict that in the future auditors will encounter less resistance to examinations of wider scope and less effort to place limitations on their work than in the past."

Implications for Legislation

The report of the New York State Attorney General had suggested that only public accountants qualified by a state board examination should be permitted to practice as public accountants. The licensing of all accountants, the report suggested, would give the state sufficient power to regulate the profession and to maintain its integrity.

The question of permissive versus regulatory legislation was still being argued within the profession. Largely because of constitutional questions the Institute had taken a stand against regulatory legislation some years before, though a number of states had adopted it.

The Attorney General's suggestion, however, stimulated reconsideration of the question. The idea evolved that if the type of practice to be restricted to licensed accountants were narrowly defined, so as to include only acts clearly affecting the public interest, principally the certification of financial statements, a law restricting such acts to those who had demonstrated their qualifications might be held constitutional. Previous court decisions had held state laws unconstitutional which restricted to licensed accountants such accounting services as public bookkeeping, drawing off of trial balances, general accounting advice, and the preparation of tax returns, which did not affect the public interest broadly.

With the approval of legal counsel, the new approach was to become the foundation of the Institute's position on accountancy legislation, and was to find its way into the laws of many states.

Extensions of Auditing Procedure

Under date of March 4, 1939, the Institute sent to all its members a confidential memorandum, analyzing the facts which had so far been developed with respect to the McKesson & Robbins case, and the line of questioning by SEC representatives in the hearings which were being conducted.

Two months later, by Herculean efforts, the special committee on auditing procedure was able to present to Council a report submitting recommendations on the examination of inventories, examination of receivables, appointment of independent certified public accountants, and the form of independent certified public accountant's report.

The committee's chairman, Patrick Glover, and Samuel Broad, who had headed the committee which prepared the 1936 revision of the Federal Reserve Bulletin, had drawn up a first draft of the proposed statement. Then revisions were hammered out at sessions of the full Institute committee. The revised draft was submitted to a "committee of 100," appointed for the purpose by the New York State Society. After a meeting which lasted nearly all night, substantial agreement was reached after a few changes. Then the report was presented at a special meeting of the state society and was approved.

Since the Institute held no membership meetings except the annual meeting in the fall, the sentiment of members was tested in several other states, and the final report was submitted to the Council, the Institute's governing body, at its spring meeting in May 1939.

All this had been accomplished in five months. The SEC had barely completed its investigation, and the drafting of its report and recommendations had just begun.

The Council approved the committee's recommendations and ordered its report to be printed and sent to all members.

With some modifications, as a result of intervening discussion, the report of the special committee was later approved by the membership at the 1939 annual meeting.

After a general preamble related to the basic responsibilities of auditors, the report recommended that it should be generally accepted auditing procedure, wherever practicable and reasonable, for the auditor to be present either in person or by his representative at the inventory-taking, and by suitable observation and inquiry satisfy himself as to the effectiveness of the methods of inventory-taking and as to the measure of reliance which might be placed upon the client's representations as to inventories and the records thereof. In this connection, the independent CPA might require a physical test of inventories to be made under his observation.

With respect to inventories in the hands of public warehouses or other outside custodians (which figured prominently in the McKesson fraud), direct confirmation in writing from such custodians was to be considered acceptable procedure, "except that, where the amount involved represents a significant proportion of the current assets or of the total assets of the concern, the independent certified public accountant shall make supplementary inquiries."

With regard to receivables it was recommended that wherever practicable and reasonable, and where the aggregate amount of notes and accounts receivable represented a significant proportion of the current assets or of the total assets, confirmation by direct communication with debtors should be regarded as generally accepted auditing procedure.

Further, it was suggested that independent auditors be engaged or nominated by the board of directors or elected annually by the stockholders and that the auditor be appointed early in each year.

Appropriate changes in the standard form of independent auditor's report or opinion were recommended at the same time. As revised, the form of report proposed was as follows:

> To the Board of Directors (or stockholders) of the XYZ Company:
>
> We have examined the balance sheet of the XYZ Company as of April 30, 1939 and the statements of income and surplus for the fiscal year then ended, have reviewed the system of internal control and the accounting procedures of the company and, without making

a detailed audit of the transactions, have examined or tested accounting records of the company and other supporting evidence, by methods and to the extent we deemed appropriate.

In our opinion, the accompanying balance sheet and related statements of income and surplus present fairly the position of the XYZ Company at April 30, 1939, and the results of its operations for the fiscal year, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

The substance of this report was published in Statements on Auditing Procedure No. 1, "Extensions of Auditing Procedure." It was the beginning of a series which served the profession well on later occasions.

The SEC Findings

The SEC hearings begun on January 5, 1939 were completed on April 25, 1939, although the final report, with recommendations and a full record of the testimony, was not published until December 1940. In all, 46 witnesses had been examined, including partners of accounting firms, representatives of the Controllers Institute of America and the American Institute of Consulting Engineers, and employees and directors of McKesson & Robbins.

"Throughout," said the SEC report, "Price Waterhouse & Co., the witnesses, and their counsel extended the fullest cooperation in facilitating the conduct of the proceedings. The record of the public hearings is contained in 4,587 pages of testimony and 285 exhibits comprising in excess of 3,000 pages."

The variety of the subject matter covered at the SEC hearings was striking. It ranged from the details of staff organization, and delegation of responsibilities in an audit, through some 50 questions on specific items of the audit program, to what might be termed the philosophy of auditing—the purpose and the meaning of an accountant's certificate, and the basic responsibility of auditors.

The SEC's final conclusions had been awaited by the profession with bated breath.

Noting that McKesson's auditors had been appointed by the president or the controller, and that the board of directors had no significant part in arranging for the audit or its scope, the Commission's report said: "While the appointment . . . and the method of determining the scope of the engagement in this case was in accord with generally accepted practice, we do not feel that it insures to the auditor, in all cases, that degree of independence which we deem necessary for the protection of investors."

It was recommended that auditors be elected by stockholders; that a committee be selected from non-officer members of the board of directors to make all nominations of auditors and to arrange the details of the engagement; that the auditor's certificate be addressed to the stockholders; and that all other reports be addressed to the board of directors and copies delivered by the auditors to each member of the board; that the auditors be required to attend meetings of stockholders and respond to questions; and that if for any reason the auditors did not complete the engagement, they should nevertheless render a report on the amount of work done and the reasons for non-completion, which should be sent by the company to all stockholders.

The report also said, "The auditor must realize that, regardless of what his position and obligations might have been when reporting to managers or to owner-managers, he must now recognize fully his responsibility to public investors by including the activities of the management itself within the scope of his work and by reporting thereon to investors."

Among other things, the report deplored the necessity for recruiting large numbers of temporary employees during the short busy season, and advocated general adoption by corporations of natural business years for accounting purposes. Better training, development, and supervision of staff was also recommended.

The report concluded that Price Waterhouse & Co. had

conformed to the prevailing generally accepted procedures for examination of financial statements, but commended and supported the action of the profession in adopting the new requirements for confirmation of receivables and physical observation of inventories, as set forth in "Extensions of Auditing Procedure." The SEC report charged, however, that the auditors of McKesson had "failed to employ that degree of vigilance, inquisitiveness, and analysis of the evidence available that is necessary in a professional undertaking, and is recommended in all well-known and authoritative works on auditing."

It was hardly to be expected that a government agency, in a case which had excited so much public attention, could let the accountants off with no criticism at all.

Most significant to the profession as a whole was the following statement in the SEC report:

> We have carefully considered the desirability of specific rules and regulations governing the auditing steps to be performed by accountants in certifying financial statements to be filed with us. Action has already been taken by the accounting profession adopting certain of the auditing procedures considered in this case. We have no reason to believe at this time that these extensions will not be maintained or that further extensions of auditing procedures along the lines suggested in this report will not be made. . . . Until experience should prove the contrary, we feel that this program is preferable to its alternative—the detailed prescription of the scope of and procedures to be followed in the audit for various types of issuers of securities who file statements with us—and will allow for further consideration of varying audit procedures and for the development of different treatment for specific types of users.

The profession had survived another crisis. The impact of this case on practice generally was highly significant. Aside from the specific requirements embodied in "Extensions of Auditing Procedure," most accounting firms quietly reviewed their own procedures and approaches in the light of the testimony at the SEC hearings. Many companies adopted the practice of having their auditors elected by the stockholders,

and audit committees of boards of directors grew more numerous.

For the first time the Institute created a standing committee on auditing procedure. Its first chairman was Samuel J. Broad, senior technical partner of Peat, Marwick, Mitchell & Co. He had been the chairman of the committee which prepared the 1936 revision of the Federal Reserve Bulletin, and had taken an active part in the Institute's activities related to the McKesson case. He became president of the Institute in 1944.

Following the example of the recently created committee on accounting procedure, the new committee on auditing procedure began the issuance of statements on auditing procedure, covering points which needed interpretation, or had not hitherto been dealt with in official pronouncements. Between October 1939 and March 1941, the committee issued six such statements in addition to "Extensions of Auditing Procedure": "The Auditor's Opinion on the Basis of a Restricted Examination"; "Inventories and Receivables of Department Stores, Installment Houses, Chain Stores, and Other Retailers"; "Clients' Written Representations Regarding Inventories, Liabilities and Other Matters"; "The Revised SEC Rule on 'Accountants' Certificates" (two sections); "Contingent Liability under Policies with Mutual Insurance Companies."

Then the United States became involved in World War II, and this committee turned its attention, as will be seen later, to matters related to the war effort.

However, the profession had again set its feet upon a new path which led to increased public confidence.

The Ethics Committee Report

In the normal course the McKesson & Robbins case came before the Institute's committee on professional ethics, which in accordance with custom deferred action until the official proceedings before the SEC had been completed. Under date

of May 12, 1941, the report of the ethics committee was presented to the Council by Dr. Joseph J. Klein of New York.

The report stated that the committee had studied intensively the published report of the Securities and Exchange Commission, and particularly the testimony of the accountants who were expert witnesses. The committee also obtained additional information about the case from other sources.

Pertinent sections of the SEC's findings were quoted at length. The committee's conclusion was as follows: "Your committee, after prolonged study and discussion, has reached the unanimous conclusion that no prima facie case of violation, either of our bylaws or of our rules of professional conduct, has been established. In the presence of such a finding, no report to Council is required, but, because of the importance of the case, we shall briefly discuss the basis of our conclusions."

The bases for formal charges against members in a case of this kind were (1) a provision of the bylaws providing for discipline of a member guilty of an act discreditable to the profession; and (2) the applicable rule of professional conduct providing for discipline of a member who certified financial statements containing essential misstatements, "upon proper presentation of proof that such misstatement was either willful or the result of such gross negligence as to be inexcusable."

The committee concluded that members could not be guilty of an act discreditable to the profession through failure to follow procedures which were not mandatory at the time of their audit. As a result of its independent investigation, the committee also concluded that the members concerned had made no willful misstatement as a result of their audit. There remained for consideration, therefore, only the question whether or not these members were guilty of inexcusable gross negligence.

Reference was made to the statement in the SEC report, quoted above, that the auditors failed to employ a sufficient degree of vigilance, inquisitiveness, and analysis of the evidence available. However, the committee's report continued:

"Your committee has spent considerable time in giving much thought to this conclusion of SEC. Whether or not the auditors

involved were as vigilant or as inquisitive as other competent auditors would have been under similar circumstances at the same time is a psychological question which your committee finds itself unable to answer, partly because it is impossible to divorce our present knowledge of the circumstances from the consideration of what other reputable and experienced accountants might have done prior to exposure of the fraud. Manifestly we could not join in this conclusion of the SEC unless we were convinced, as we are not, that the criticism is well-founded. Your committee has made prolonged and careful study of all the evidence available; it did not find, in its opinion, evidence warranting the conclusion that the members concerned were careless or indifferent in the conduct of their work, and certainly in no such degree as would have to be shown to exist in order to justify charges of 'inexcusable gross negligence' under the Institute's bylaws."

In view of the unusual importance of this matter, a partner of Price Waterhouse & Co., Rodney F. Starkey, had been invited to appear at the Council meeting where the report of the committee on professional ethics was presented. He volunteered to answer any questions. Presidents of state societies and committee chairmen who had the privilege of the floor at the meeting were invited to participate in the questioning.

Mr. Starkey responded to a number of questions. Members of Council commented on various points developed in the questioning. At the conclusion of this period, on a motion duly seconded, the report of the committee on professional ethics was approved.

Concern was expressed, however, that the membership generally might suspect that the Institute was shielding a prominent firm. Clem W. Collins, a recent president of the Institute, said:

> Ever since this matter came up, which is about three years ago, there have been numerous criticisms. When I was president, I received a great many letters insinuating that there was not full consideration being given, and that because this firm was a large firm, perhaps they were not subjected to as severe examination and cen-

sure as might be accorded to a smaller firm. Continually I am hearing things said. Even last night the president of a state society suggested that there had not been a full consideration of the case . . . . I feel quite strongly that when we have settled this, it ought to be considered settled, and certainly no one present has a right to go out and make any claim that it had not had full and complete consideration if he fails to make himself heard at this time. If he sits silent and says nothing, then I think that he gives, by his silence, consent to the action.

There was discussion of the possibility of publishing a full statement of the facts for the information of the membership. It was pointed out that throughout the period in which the matter had been under consideration the members had been kept currently informed of the essential facts in the case. Finally the executive committee was given discretion to publish any additional statement on the matter which seemed desirable. The executive committee later concluded that the report of the ethics committee spoke for itself, and that report was published in full in *The Journal of Accountancy* for July 1941.

The McKesson case had been an abrasive experience for the profession as a whole—especially for those then in charge of the Institute's affairs—and most of all for the partners of the eminent accounting firm involved. Yet, if it cannot be said that the profession emerged with flying colors, it did come out of the affair without permanent injury. In fact, the results, in the long run, strengthened the profession's position. The importance of independent audits, and their unavoidable limitations, had been brought forcefully to the attention of many people who had given little thought to the matter before. The constructive work resulting in Statements on Auditing Procedure No. 1, "Extensions of Auditing Procedure," led to a series of authoritative pronouncements on auditing standards and procedures, which, as will be shown in Chapter 7, greatly strengthened the position of independent auditors.

CHAPTER 3

War Years

WHILE the accounting profession in the United States was struggling with its internal problems and enduring its growing pains, powerful and destructive forces were building up in Europe and Asia. Nazi Adolf Hitler was threatening Europe. Fascist Mussolini was rattling his saber in Africa and the Balkans. Japan was involved in undeclared war with China. Stalin's Russia sought to make the whole world communist.

International tensions were building up to a point at which the United States could not escape involvement, with unpredictable impact on all its institutions, including the accounting profession.

As always, the people of the United States were extremely reluctant to be drawn into another war. But when Hitler invaded Poland in September 1939, and Great Britain and France declared war on Germany, sentiment in the United States began to change. After the stunning defeat of France, and the escape of the British at Dunkirk, President Roosevelt announced, "We

will extend to the opponents of force the material resources of this nation; and, at the same time . . . speed up the use of these resources in order that we . . . in the Americas may have equipment and training equal to the task of any emergency." The United States began to supply munitions to the British.

While the pacifist attitude was still strong in the United States, an increasing number of citizens began to believe that only by helping Britain would America be saved from ultimate attack.

Defense Preparations

In September 1941, three months before Pearl Harbor, the American Institute of Accountants held its annual meeting in Detroit. The retiring president, C. Oliver Wellington, in his address reflected the general awareness that entry of the United States into the war was not far away.

> We don't like war. No one likes war. But what will be the result of our lives and the lives of our children if we allow the international gangsters to grow stronger and stronger?
>
> . . . In addition to our responsibility as citizens, we have a duty to help clients in adapting their financial and operating policies to the new conditions. Shortages of materials necessary to defense will require increased civilian rationing of commodities, with consequent distress to some businesses; inflation will cause rises in the prices of practically all materials, labor, and services; higher and higher taxes will induce economic dislocation and much hardship. . . . The accounting profession can help the government by suggesting the easiest, most convenient, and least expensive methods of taxation, the most effective control over expenditures, and the best safeguards against waste or loss. . . . In war, as in peace, the accountant is bound to be an indispensable part of the economic machinery.

At the same annual meeting a resolution was adopted, on recommendation of the committee on national defense, calling on government to make the most effective use possible of per-

sons with accounting training who might be inducted into service under the Selective Service Act.

The defense committee reported that it had co-operated with the Advisory Commission to the Council on National Defense. A questionnaire had been issued to all members of the Institute, to which more than 500 replies were received, providing information as to the availability of members for defense work of various kinds without compensation. Ten of the committee's 19 members had been called upon for service in the defense program. At the request of the War Department, a subcommittee had reviewed audit manuals prepared for the guidance of field auditors under the Quartermaster Corps in connection with construction projects. Advice had also been offered to the Advisory Commission on the possibility of co-ordinating the audit procedures of the several defense agencies.

The Institute's staff had responded to numerous calls for accounting personnel required in the defense program and was setting up a record of services being rendered by members of the Institute in the armed forces or in other defense capacities.

Three members of the defense committee were serving as dollar-a-year men in the Office of Production Management. One of the Institute's vice presidents was engaged in a special assignment for the Export Control Board. Five prominent members of the Institute were manning the accounting and auditing section in the office of the Under-Secretary of War. Another member of the committee was serving as special assistant to the Paymaster General in the Navy Department. Several other members were serving on a special panel of advisors to the War Department dealing with problems related to amortization of investment in defense-plant facilities.

Some Institute members had been called to active duty as reserve officers or members of the National Guard.

The Institute was also collaborating with the government in drafting a questionnaire for accountants as a part of a nationwide survey of technical, scientific, and professional personnel in conjunction with the defense program.

Pearl Harbor

Norman L. McLaren was elected president of the Institute to succeed Mr. Wellington. Mr. McLaren was senior partner of the firm of McLaren, Goode & Company in San Francisco. He had been an active participant in Institute affairs over a period of years, serving as a member of the Council and various committees, and currently the committee on national defense.

On December 7, 1941, President McLaren and the secretary of the Institute were relaxing in the lounge of a Pullman car headed west, where they were to fulfill speaking engagements at state society meetings. Over the radio came the news of the Japanese attack on Pearl Harbor. After a period of shocked silence, Mr. McLaren said, "This means war. I am going into uniform."

Shortly after, he was sworn in as an officer of the United States Navy with the rank of commander, and later was promoted to captain, serving as chief of the cost and audit division of the Office of Procurement and Material. He offered to resign as president of the Institute, but the executive committee rejected this offer. Mr. Wellington, the immediate past president, was named as acting chairman of the executive committee, to preside at meetings which the president might be unable to attend.

Other members of the Institute, too numerous to name, joined the armed services. Among the most prominent was Colonel Arthur H. Carter, a West Point graduate, who became a major general in the Army and director of the fiscal division, Army Service Forces.

At the 1942 annual meeting the principal topic of discussion was war problems. Among the members participating were the following: Colonel Andrew Stewart, Lt. Colonel John W. McEachren, Lt. Colonel H. W. Burrows, and Lt. Colonel Morris C. Troper, all of the War Department; Paul Grady, who as a civilian headed the cost inspection service of the Navy Department, and Lt. Leslie Mills, who was engaged in

renegotiation work for the Navy. Professor T. H. Sanders, who, though not a member, had been the Institute's research director, became chief of the cost-analysis section, purchases division, War Production Board. J. Harold Stewart, who became president of the Institute in 1949, also served as a captain in the Navy.

In his presidential address at the 1942 meeting, Commander McLaren reflected the uneasiness of the American people, as the war was not going well:

> Day by day it becomes more apparent that ultimate victory in the war hinges upon the productive ability of the American people. The progress that has been made in our conversion to a complete wartime economy is gratifying, but our job is just begun. . . . There is no place in this fight to the finish for the weak, the sentimental, and the nonproducer. The part which must be taken by our profession is crystal clear—individually and collectively we must demonstrate that in war, as in peace, we are eager and fully prepared to do all that our country has the right to expect of us. . . . Our younger members by the thousands are responding to the call to the colors. . . .

He referred among other matters to the panel of supervising auditors under the cost and audit branch of the Navy, including approximately 150 members of the Institute representing every section of the country.

George S. Olive, senior partner of Geo. S. Olive and Company, Indianapolis, was elected president of the Institute to succeed Commander McLaren.

The Institute had turned almost all of its energy toward war activities.

Accounting Manpower

While refusing to recommend blanket deferments of accountants from military service, the Institute did make efforts to conserve enough trained accounting manpower to meet the

needs not only of the military and civilian war agencies, but also the producers of goods and services essential to the war effort and the civilian economy.

Young staff accountants and college students who might have become staff accountants were entering the armed services by the thousands. Public accounting firms were having difficulty in obtaining deferments even of older experienced CPAs who were engaged in essential work.

The first approach by an Institute representative to the Selective Service System resulted in a meeting with a Navy commander who had been assigned to that service. His first reaction was, "I am allergic to accountants." He had been a practicing lawyer who shared the feeling prevalent in some quarters of the Bar that accountants were invading the practice of law in their tax activities (see Chapter 9).

However, after persistent efforts with both Selective Service officials and the War Manpower Commission, rulings were obtained that accountants possessing training and skill of professional quality who were engaged in essential activities were entitled to consideration for deferment. But, local draft boards were given wide discretion in applying Selective Service directives, and many accounting firms were unsuccessful in seeking deferments even for key men.

By 1944, however, the government's approach had been altered. Deferment of registrants of the ages 18 through 25 was so tight that occupational grounds were virtually eliminated. Registrants of ages 26 through 29 could be considered for occupational deferment under the criteria theretofore issued, while registrants of ages 30 through 37 benefited from material relaxation of the requirements for occupational deferment.

Institute committees and staff spent hours, days, and weeks in Washington and elsewhere on various aspects of the manpower problem—recruiting competent accountants for the military and civilian war agencies, attempting to secure deferments for CPAs who were doing essential work, and trying to have skilled accountants in the armed services assigned to

tasks where they could do the most good. A continuous flow of information on these matters went to the state societies and the membership as a whole.

Consulting Activities

The committee on war activities and other Institute groups were busily engaged in responding to inquiries on accounting or auditing matters upon which war agencies needed professional advice.

Under General Accounting Office requirements, costs incurred under cost-plus-fixed-fee contracts had to be preaudited—that is, each item of expense had to be checked and approved at the time it was incurred—in order to provide a basis for reimbursement of the contractor. Efforts were made to change this policy to permit post-audit of contractors' costs.

Advice was given the executive director of the Supply, Priorities and Allocations Board on the major problem of allocating materials between defense and non-defense industries.

Institute representatives reviewed procedures followed in the audit of Army Post Exchanges, which resulted in an audit manual for this purpose.

Co-operation was given the War Production Board in a study designed to facilitate elimination of duplications in questionnaires sent by war agencies to industrial companies.

At the request of Army officers a special committee undertook to review and co-ordinate the audit manuals utilized by the several branches of the Army.

The War Department eventually approved selective auditing procedures in the audit of contractors' accounts, instead of the traditional requirement of a detailed check of all items.

Advice was given on interpretation of cost criteria applicable to cost-plus-fixed-fee supply contracts.

Institute representatives reviewed drafts of a War Depart-

ment manual for administrative audit of termination claims of fixed-price supply contractors.

Renegotiation was another area in which many accounting questions were involved. Carman G. Blough, formerly chief accountant of the SEC, had taken a post with the War Production Board as liaison member of all price-adjustment boards. With his co-operation an Institute committee was enabled to make policy recommendations on renegotiation.

The committee on federal taxation made countless recommendations on legislative proposals, as well as administrative policies, related to wartime taxes. It was instrumental in securing extensions of time for filing tax returns in order to lighten the burden on taxpayers caused by the shortage of accounting manpower. It also persuaded the Bureau of Internal Revenue to maintain a reasonably flexible policy in permitting changes from calendar-year to fiscal-year closings, which minimized the peak-load pressures on accountants, as well as on the personnel of the Bureau itself.

Technical Activities

During the war years the committee on auditing procedure issued statements on auditing under wartime conditions, disclosure of the effect of wartime uncertainties on financial statements, physical inventories in wartime, confirmation of receivables from the government, termination of fixed-price supply contracts, and wartime government regulations.

The committee on accounting procedure issued research bulletins on accounting for special reserves arising out of the war, United States Treasury notes, post-war refunds under the Revenue Act of 1942, accounting for cost-plus-fixed-fee contracts, reserves for possible renegotiation refunds, and accounting for terminated war contracts.

The technical committees were handicapped by the lack

of adequate staffs. Victor Z. Brink, who had been assisting the committee on auditing procedure, became a lieutenant colonel in the Army. His work was taken over by George Farrand, who had been an assistant in the research department, until he, too, obtained a commission in the Navy.

Keeping the Members Informed

Massive amounts of information were sent to members of the Institute during the war years, not only through *The Journal of Accountancy* and *The Certified Public Accountant,* but in special reports and proceedings of the annual meeting. Such information varied from rules on gasoline rationing and Selective Service regulations to highly technical requirements affecting industries providing material to the government.

In addition, while transportation was difficult and meetings had to be curtailed, Institute officials travelled with great difficulty to various parts of the country for face-to-face discussions at meetings of state societies on problems with which the profession was struggling.

Owing to a shortage of paper, the size of *The Journal of Accountancy* was curtailed somewhat. Publication of the 1942-43 *Yearbook* was omitted and the 1943-44 edition was condensed.

The 1945 annual meeting was cancelled because of transportation problems and the unavailability of adequate hotel accommodations. Instead, a two-day meeting of Council was held in Chicago, to which presidents of state societies, committee chairmen, and representatives of other accounting associations were invited. Elections and other official business were conducted via mail ballots to the entire membership.

So extensively were the Institute's resources and energies devoted to war-related activities that the War Manpower Commission officially declared it to be an "essential organi-

zation" under the regulations. This was an unusual distinction for a non-profit membership association.

The Institute's Organization

When the United States entered the war the Institute's staff numbered 43 persons, including the director of research and one research assistant who were on a part-time basis. By the spring of 1943 the number had dropped to 32. Five former staff members were serving in the armed forces, and others had left for other reasons. Through strenuous recruiting efforts, replacements were found, and by the end of the war the total number had grown to 47, an all-time high.

Somewhat to the surprise of the Institute's officers, the membership continued to grow throughout the war. From 5,722 in 1941 it grew to 9,051 at the end of the fiscal year 1944-45. Likewise, the circulation of the *Journal* increased from 15,684 to 25,573.

While the war years were an ordeal for all concerned, especially those in active military service, the profession as a whole emerged from them stronger in every way than it had been before.

The ordeal was reflected in the address of George S. Olive as president at the 1943 annual meeting:

> Those of us left in public practice have been loaded with more complicated questions on which clients have needed our help than have been presented since 1918—the intricacies of renegotiation, wage stabilization, excess-profits-tax computations and plans for relief therefrom, victory tax, withholding tax, declarations of estimated tax liability, and trying to convince clients that Congressional talk of forgiveness of a portion of the 1942 or 1943 tax really had the results of increasing their taxes for the current year rather than reducing their liabilities. With personnel much reduced and work greatly increased, we have all tried to stretch out the hours and render the best service possible.

Victor H. Stempf, a partner of Touche, Niven & Co. in New York, succeeded Mr. Olive as president. At the end of his arduous year in office, he brought the following words to the 1944 annual meeting:

> Statesmanship in the profession looks beyond immediate selfish interest or expedience toward the long-range development of the influence, recognition, and prestige of the profession, through unmistakable service in the public interest. . . . It demands an awareness of opportunity and a willingness to act promptly, fearlessly, and diligently, as have all of the Institute's special wartime committees during the past three years. . . . We are becoming more sharply aware that accounting is a potent social force; that its use or abuse may radically affect the destiny of our economy.
>
> As the profession grows in influence, as it gains public respect and recognition, so will it also become more and more the target of attack, either by those jealous of its preferment or by the drooling wolves before an imagined strike-suit feast. We must guard our right to determine what are generally accepted accounting principles and generally accepted auditing standards. As a profession, we have an inalienable right to set for ourselves objective standards of independence, integrity, and competence.

Mr. Stempf was the only man to have served as president of the three largest accounting organizations in the country—the New York State Society of Certified Public Accountants, the National Association of Cost Accountants, and the American Institute of Accountants. His influence was widespread.

Aftermath

Samuel Broad of Peat, Marwick, Mitchell & Co., New York, succeeded Mr. Stempf as president. His tireless efforts on behalf of the profession have been recited in the preceding chapter. Throughout the war years, he had served as chairman of the committee on auditing procedure.

In his report to the members in the fall of 1945, Mr. Broad said:

> The accounting profession has had an important part to play in the war effort and will continue to play an important part in dealing with the economic problems which constitute a major part of the aftermath. . . . More and more it becomes evident how fortunate we are as a professional organization in having so many men with ability and the qualities of leadership ready, even eager, to place their services at the disposal of the profession. Perhaps it is because we are a young and progressive profession and we all feel that we are going places. Be that as it may, the steady and concerted work of our committees, ably supplemented by the staff, shows in the significant gains our profession is making in prestige and public esteem as the years go by. . . .
>
> The economic struggles which have characterized western civilization for the past centuries seem to be reaching a new peak. The benefits from new inventions, from war-accelerated improvements in manufacturing processes and machinery, and from lower production costs, should be shared equitably among labor, management, consumers, and the owners of the business. . . . There are wide differences of opinion on this point and it seems logical that the first step toward reaching an agreement should be to determine what are the underlying facts. We as accountants should, I believe, be able to be helpful in reporting what the underlying facts are, provided we can convince the parties as to our independence of viewpoint.

The influx of accountants into Washington during the war, and their participation in war-related activities in all parts of the country, plus appearances of Institute representatives at hearings before Congressional committees and in conferences with high officials of the military and civilian war agencies had all given the accounting profession more visibility than it had enjoyed before. Acquaintances were formed with leaders from other fields of endeavor who were sharing the management of the war effort. And these friendly relations persisted for many years thereafter.

In addition, the members of the profession had perhaps acquired increased self-confidence as a result of wartime experiences. They found that they could hold their own—and

sometimes do better than that—in discussions with top-level leaders from other disciplines.

Wartime manpower shortages forced accounting firms to economize as much as possible in the expenditure of man-hours. This led to intensive study of ways to use staff to best advantage. A more analytical approach to auditing resulted. Unnecessary detailed checking was avoided. Carefully selected samples for audit tests became more prevalent. It was found that much audit work could be performed prior to the year-end, and the phrases "interim auditing" and "continuous auditing" began to come into usage.

Women were engaged as staff assistants on a larger scale than ever before, and many of them remained in the profession after the war. It was, in fact, wartime necessity which broke down to a large extent the prejudice against women in accounting which had existed before. Thereafter their numbers grew quite rapidly, and it became no longer unusual for women to be assigned to audit staffs.

Management Services

Perhaps the most important impact of the war on the practice of public accounting was the application of mathematical and systems approaches to the logistics problems of the military.

At the outbreak of World War II in England, scientists were called to the assistance of the Air Force to attack the critical problem of co-ordinating the newly developing early-warning radar system with Air Force operations. This in turn led to investigations of the efficiency of the total communications systems. Similar systematic approaches were applied later to other military problems and came to be designated as "operational research."

After the war, operations-research techniques were added to the tools developed during the "scientific-management" era

of the preceding years. Their scope was expanded by the advent of computers. Operations research, alternatively called "management sciences," began to be used in industrial companies on an increasing scale.

Accounting firms did not ignore these developments. Not long after World War II, they began to offer "management services" as a separately identified branch of accounting practice. These services differed little in purpose from the cost accounting, systems work, and advisory services which accountants had been offering clients for decades. But the new mathematical techniques and data-processing facilities enabled such services to be rendered at a higher level of sophistication and often at less cost than would have been possible without the new tools.

This field of management advice and assistance became a steadily increasing proportion of the total volume of public accounting services.

The officers of the Institute approached the post-war years with optimism.

"The country may soon be thinking in terms not of restriction, but of expansion, full employment, full production, new outlets for human activity," said the secretary in his 1945 report. "Problems of a nature quite different from those of the past three years may soon confront the accounting profession. The Institute, as the profession's instrument for collective action on the national scale, should be geared to deal with these problems as well as possible."

Plans and programs were laid out for the years ahead, embodying increased activity in the field of research, personnel recruiting, adult education, public information, and many other areas. The period of explosive growth of the profession and of the Institute was soon to begin. With it came new and painful problems.

CHAPTER 4

Pressure for Comparability Of Earnings

As World War II drew to a close, fears were expressed about what might happen to the economy when peace prevailed again. Memories of the depression were still fresh in mind. Would a sudden drop in the production of war munitions throw millions of people out of work? Would the millions of returning servicemen added to these mean widespread unemployment, bread lines, and soup kitchens?

Henry Wallace, Vice President of the United States under Roosevelt prior to the 1944 election, wrote a short book, *Sixty Million Jobs,* urging the government to take steps to assure enough work for the people.

A Congressional committee, the Temporary National Economic Committee, heard learned professors testify that the U.S. economy had matured, that capitalism had reached the end of its frontiers, and that the country could not look for-

ward to an expanding economy, but rather had to reconcile itself to an equitable division of the wealth already available.

What actually happened astonished even the optimists. Industry converted quickly from production of war material to production of consumer goods. The strong pent-up demand for goods and services, restrained by wartime shortages and controls, provided an eager market for all that industry produced. Returning servicemen were easily absorbed into industry, or into educational institutions, supported by the G.I. Bill of Rights, which equipped millions of them for jobs on a higher level than they could have attained before. The accounting profession, incidentally, was one of the beneficiaries of this farsighted program to provide higher education for returning servicemen.

Before long there were 70 million jobs, not just the 60 that Wallace had demanded and that many had thought a hopelessly optimistic target.

In short, the country embarked on an economic boom which, with only minor interruptions, continued to the time of this writing. Heavy doses of inflation accelerated expansion of the economy at unprecedented speed. One aspect of the expansion of crucial importance to the accounting profession was the development of "people's capitalism."

Industry needed massive amounts of capital to expand plants and equipment, which in turn created many new jobs and thereby infused the economy with even more purchasing power. The best way to raise that capital was to tap the savings of the people directly. This was done by encouraging investment in common stocks by people of moderate means. Under the banner of "people's capitalism," the stock exchanges actively promoted such investment.

For those who did not care to buy stocks directly, the mutual funds offered opportunity to get into the stock market by proxy, through periodic payment of what an investor could afford.

Institutions also began to invest in equities more heavily than before the war, when bonds had been considered appro-

priate for trust funds of all kinds. As the pace of inflation quickened, common stocks offered a better chance of being paid off, through capital gains, without erosion of purchasing power. Consequently, insurance companies, pension funds, universities, executors of estates, and private organizations of all kinds—including the American Institute of Certified Public Accountants—steadily increased the proportion of equity securities in their portfolios.

These institutions, be it noted, were also custodians of the savings—unspent dollars—of various segments of the public.

In 1940, it had been estimated, there were about four million stockholders in the country. Even among this number, there was a heavy concentration of holdings in the hands of a relatively few wealthy people and institutions. But by 1952 the number of stockholders was approaching seven million, by 1962 it hit 17 million, in 1965, 20 million, and in 1968 about 24 million, with no sign of faltering.

In one way or another, a large proportion of the American people had a direct or an indirect financial stake in the stock market. The economic, political, and social implications of this situation were of unparalleled magnitude. Private investment decisions became a matter of national importance.

Focus on Earnings Per Share

How were these decisions made? Relatively few investors were equipped, or had the time, to make a thorough analysis of the financial statements, with footnotes, of the companies whose common stock they intended to buy—to say nothing of the equally important non-financial considerations affecting the earning power of such companies: the quality of management, shifts in market demands, changes in technology, and many other factors.

The traditional formula for valuing common stock was to apply a multiple to earnings per share. If earnings per share

were rising steadily from year to year, a higher multiple was considered justified; in other words, prospective higher earnings warranted a higher immediate price. On the contrary, declining earnings would suggest a lower multiple.

How were earnings per share determined? Obviously by dividing reported net income by a certain number of shares.

Thus the net income figures appearing in corporate financial statements, audited by independent certified public accountants, became a matter of national importance. And so the accounting principles on which net income was determined attracted more attention from the general public and its spokesman, the press, than ever before in the history of the accounting profession.

The emphasis in most discussions of the subject was on "uniformity," or, as most CPAs preferred, "comparability," of reported earnings of different companies. Since a decision to sell a stock, buy it, hold it, or sell it and buy another was based largely on reported net income figures, it naturally appeared important to most investors that those figures be based on accounting principles which would permit valid comparisons of the net income of one company with that of others.

The result was increasingly heavy pressure on the accounting profession—specifically the American Institute of Certified Public Accountants—to eliminate alternative methods of accounting for similar transactions which made such comparisons unnecessarily difficult, if not impossible.

This mounting pressure came principally from five sources: the SEC, the American Accounting Association, the financial analysts, the financial press, and elements within the Institute itself.

However, powerful countervailing pressures also developed among some corporate managements and organizations representing them, such as the National Association of Manufacturers, and the Financial Executives Institute (formerly the Controllers Institute of America).

The Institute found itself in the middle—as one observer put it, "in the eye of a hurricane." A weaker organization

might have panicked and, by trying to please everyone, have compounded confusion. Or it might have abdicated responsibility and run for cover. The Institute, however, resisted the pressures from both sides, and conducted an agonizing reappraisal of its own position, which resulted in adoption of new goals, new procedures and new sanctions. This was not accomplished without internal stresses and strains.

Pressure From the SEC

The Securities and Exchange Commission always had the power to prescribe accounting rules of all types for companies subject to its jurisdiction. The Commission, however, refrained from attempting to prescribe uniform accounting principles for industrial and commercial corporations, although it did prescribe uniform systems of accounts for companies subject to the Public Utility Holding Company Act of 1935 and for brokers and dealers. Under the Investment Company Act of 1940, also, the Commission issued rules providing, as authorized by the Act, for "a reasonable degree of uniformity in the accounting policies and principles to be followed by registered investment companies in maintaining their accounts, and in preparing financial statements required pursuant to this title."

For the general run of companies issuing securities to the public, however, the Commission relied on a case-by-case approach in exercising its authority, as noted in Chapter 1.

Generally, the Commission enforced the Accounting Research Bulletins of the Institute's committee on accounting procedure through deficiency letters or informal conferences with officials of corporations who filed financial statements deviating from the committee's recommendations. In rare instances the SEC disagreed with an Institute pronouncement and refused to back it up.

On several occasions where the Institute had not yet issued a pronouncement on a controversial point, the SEC took

the initiative by issuing an Accounting Series Release which, in effect, had the authority of a rule.

Keenly aware of their own responsibility for the protection of investors, and of their own vulnerability to criticism, some Commissioners and chief accountants expressed impatience with delays in the Institute's efforts to resolve important questions; and within the Commission, from time to time, consideration was given to the desirability of enunciating comprehensive accounting rules under its general statutory authority.

Speeches by chairmen and members of the Commission and by its chief accountants sometimes sharply criticized the accounting profession and sometimes warmly praised it. Whether the carrot or the stick was used, however, there was always pressure on the Institute to do more, and to do it faster, in narrowing the areas of difference in accounting practice.

After only four years of experience with the Securities Act, Commissioner George C. Matthews, in 1937, expressed some uneasiness about the effectiveness of the permissive approach to the development of accounting principles. He said that where the accounting profession gave evidence of its capacity and willingness to develop and apply proper methods without evasion or undue delay, it should be encouraged to take on the responsibility. However, while acknowledging that some progress had been made, he suggested that there were obstacles to early resolution of the numerous problems that remained unsolved. Among other things, Mr. Matthews referred to "manifestations of environmental influences in the work of accountants before us"—a tendency to rely on precedent and authority rather than on the scientific method. On this point he said, "The competitive nature of the profession and its traditional affiliation with management make the acceptance of precedent dangerous. . . ."

Remarks of this kind were often the result of specific cases which had come before the Commission. In one case, for example, while all the Commissioners disapproved the accounting, the majority believed that there had been adequate

disclosure by footnote or otherwise so as to comply with the statute and make a stop-order proceeding inappropriate.

As a result of such incidents, however, a major policy decision of the Commission was reflected in Accounting Release No. 4 issued in April 1938. This stated, in effect, that where financial statements were prepared in accordance with accounting principles for which there was no "substantial authoritative support," such statements would be presumed to be misleading or inaccurate despite disclosures contained in the certificate of the accountant or in footnotes to the statements, provided the matters involved were material. The release further provided that even where there might be substantial authoritative support for the practices followed, they would not be acceptable if the position of the Commission had previously been expressed to the contrary in rules, regulations, or other official releases, including the published opinions of the chief accountant.

In commenting on this release, William W. Werntz, the chief accountant, said in a speech to the Controllers Institute, "In view of the contradictory practices which at the present time have substantial support, it is to be hoped that any statement of principles that is finally formulated will not permit of such flexibility in application as to destroy the basic comparability of financial statements resulting from their application to business transactions of different issuers." This was an early official reference to the goal of comparability.

In 1939 Mr. Werntz said in another address that "much can be done in the way of making uniform the principles followed in the preparation of the statements. Accounting statements are intended to convey information. In this sense accounting is a language. Therefore, sufficient similarities must be obtained between the financial statements of comparable companies to enable the reader to make comparisons without first having in hand a separate dictionary and grammar book for each of the companies. Like a language, the utility of accounting increases as its principles and definitions become standardized."

In still another address in the same year he said, "There are, I think, a large number of instances in which conflicting methods have received support under circumstances that result in confusion and invite criticism on the part of the lay reader if not the trained accountant."

In 1939 also, a significant SEC ruling emerged from the *Interstate Hosiery Mills* case, in which it was stated that the management of a company subject to SEC jurisdiction had the primary responsibility for the financial information filed with the Commission. The Commission said:

> The fundamental and primary responsibility for the accuracy of information filed with the Commission and disseminated among the investors rests upon management. Management does not discharge its obligations in this respect by the employment of independent public accountants, however reputable. . . .
>
> Accountants' certificates are required not as a substitute for a management's accounting of its stewardship, but as a check upon that accounting.

The emphasis in the case was on auditing, not accounting. The Commission outlined the responsibility of independent auditors for appropriate supervision of staff and for the review of working papers resulting from the audit.

However, this holding also encouraged the prevalent belief that management had primary responsibility for the selection of accounting principles and that the auditor's responsibility in this regard was only to satisfy himself that such principles were "generally accepted" or, in SEC terms, had "substantial authoritative support."

As the work of the Institute's committee on accounting procedure began to produce tangible results (see Chapter 1), criticism and exhortation by SEC representatives began to be tempered with commendation. Jerome N. Frank, then chairman of the SEC, said to the American Institute at its annual meeting in 1940:

> I feel that we on the SEC and you in the accounting profession can take pride in our constant efforts to improve the standards of

corporate reporting. I feel confident that we have already made a contribution so substantial that, even if the securities laws were to become a dead letter, corporate reporting would never again shrink to its former status. The stature of your profession has grown immeasurably in the past few years. Your increasing independence is the envy of other professions. Neither you nor we will ever attain perfection, but I anticipate that we will spend a good many more years on our joint effort to improve the quality and value of information to security holders.

At the next annual meeting of the Institute, Chief Accountant Werntz was a speaker. Referring to the need for authoritative expressions of fundamental concepts of accounting, he said:

> Now concrete results are appearing. The difficulties are well recognized and great. The formulation of propositions possessing wide applicability is hampered by the variety and complexity of the business events with which accounting is concerned. Furthermore, the evolution of accounting, until recently, has been heavily, indeed too heavily, pragmatic, producing a structure with internal inconsistencies which have, nevertheless, been firmly cemented in place through long usage. . . .
>
> In spite of these difficulties, the past year has seen an important contribution in the recent revision by the executive committee of the American Accounting Association of its "Statement of Accounting Principles Underlying Corporate Financial Statements."[1]

Mr. Werntz described this statement as a consistent and clear expression of accounting fundamentals—criteria by which the propriety of solutions of specific questions might be measured. He went on to say that the American Institute had approached the same objective—the improvement of accounting—by dealing directly with specific problems: "Such activity is of first-rank importance, and the statements on accounting principles contained in the research bulletins have been significant contributions . . . . It may be hoped that the flow of

[1] This was the first revision of the "tentative" 1936 statement by the American Accounting Association described in Chapter 1.

both kinds of statements and the discussion they engender will rise rather than subside."

All-Inclusive vs. Earning-Capacity

After World War II, no longer preoccupied with special problems arising out of the war economy, the SEC focused attention on the purpose of the income statement and the contentions of those who supported the "all-inclusive" statement or the "earning-capacity" approach.

Mr. Werntz concluded that no generally agreed-upon criteria existed as to when an item might properly be excluded from the income statement; that accountants had been willing to certify statements excluding some items, either on the basis that they conformed to their own views, or on the ground that in the absence of effective criteria they were unable to object; that by a choice between income and surplus it was possible to vary reported earnings within very wide limits; and that practice in the field was so devoid of any unifying principle as to be readily susceptible of misuse and misunderstanding, to the very probable detriment of investors not expert in accounting matters.

Debate persisted for several years on the all-inclusive versus the earning-capacity income statement. The latter involved direct charges and credits to surplus of material items unrelated to operating results. George D. Bailey, who had become chairman of the committee on accounting procedure, was a strong advocate of "sharpening net income." Mr. Bailey was then one of the senior partners of Ernst & Ernst and head of its important Detroit office. He had had a long and rich experience in accounting, and, in addition, was well informed on economic, political and social trends. He was studious, imaginative and energetic—an unusual combination of thinker and

activist. He had a casual, informal, pleasant manner which concealed a will of iron.

He believed that net income should reflect earning capacity —earnings from the regular business of a company, exclusive of windfalls such as gains on the sale of a plant—and should be determined in a way that would permit comparison of results of one year with those of another, and the results of one corporation with those of others, against the backdrop of the economic conditions of the times. Properly applied, this approach would facilitate comparability of earnings per share.

Over strong internal opposition, this concept was embodied in Accounting Research Bulletin No. 32 and was defended by Mr. Bailey, who had then been elected president of the Institute, in an article in *The Journal of Accountancy* for January 1948.

This bulletin, however, evoked a prompt response from Earle King, who had succeeded Mr. Werntz as chief accountant of the SEC. Mr. Werntz had resigned his post in the Commission to join the accounting firm of Touche, Niven, Bailey & Smart, organized shortly before by the same George Bailey. Mr. King argued that the procedures recommended in the bulletin "seem to be susceptible to abuse, and may result in misleading income and earned-surplus statements in conflict with published rules and opinions of the Commission as well as opinions of the chief accountant." Mr. King also announced that the Commission had authorized the staff to take exception to financial statements which appeared to be misleading, even though they reflected the application of Accounting Research Bulletin No. 32.

Samuel J. Broad had followed Mr. Bailey as chairman of the committee on accounting procedure. In the first report of the committee issued under his leadership, reference was made to the controversy over Bulletin No. 32: "This controversy has not been resolved by the issuance of the bulletin. Since governmental agencies frequently rely on form rather than substance, and since the all-inclusive concept is much easier to administer, it is to be expected that pressure will continue

to be exerted in favor of the all-inclusive concept in reporting net income."

It appeared to many CPAs that the SEC was obstructing a step in the direction of comparability of earnings, despite its frequent exhortation to move in that direction.

In 1950, the SEC circulated for comment a draft of a proposed amendment to its Regulation S-X. One proposal was in direct conflict with Accounting Research Bulletin No. 32. It would have required that all items of profit and loss given accounting recognition during a year be included in the determination of net income—in other words, making the "all-inclusive" concept a rigid requirement.

This direct contradiction of the committee on accounting procedure was greeted with indignation by Institute spokesmen. In his address at the Institute's 1950 annual meeting, J. Harold Stewart, retiring president, stated as a major problem of the profession "the indication that government agencies are leaning toward the imposition of rules which would establish accounting principles, rather than leaving the establishing of accounting principles to natural development by business and the accounting profession."

Resolutions opposing the SEC's proposed requirement were adopted by the Council and by the membership at that annual meeting.

Subsequently, a special Institute committee discussed the problem with the Commission and reached a compromise solution on the form of income statement: any special items of profit and loss given recognition in the accounts during the period, but excluded in the determination of net income, were required to be included at the bottom of the income statement after the figure of net income or loss. Such special items were required to be added to or subtracted from net income, producing a final figure to be captioned "Net Income and Special Items."

The committee on accounting procedure tentatively concluded that this form should be considered acceptable. Something new and useful to investors had been added.

Price-Level Accounting

Concurrently with the debate over the "earning-capacity" income statement, another controversy raged on the subject of "price-level depreciation."

As the purchasing power of the currency shrank with the increasing rate of postwar inflation, depreciation charges based on dollar costs did not reflect the attrition of fixed-asset values in terms of current purchasing power. Accordingly it was contended by many accountants that profits were overstated.

George O. May was in the vanguard of those who advocated conversion of depreciation charges to "current dollars" by the application of an appropriate index of price-level changes.

Others, however, had grave doubts about the wisdom of this proposal. It recalled the "replacement-cost" accounting of earlier years, which had permitted manipulation of profits by "writing up" and "writing down" fixed assets. The validity of existing price-level indices as a substitute, in effect, for actual dollar costs as a basis for depreciation was questioned. Investors might be confused by financial statements presented in terms of "might-have-been" dollars instead of actual disposable dollars. So the negative arguments ran.

George Bailey, at this time senior partner of Touche, Niven, Bailey & Smart, emerged as one of the leaders of this camp. The SEC also let it be known that it had no enthusiasm for price-level depreciation.

There were sound and persuasive arguments on both sides, however, and there was no doubt that the subject was important enough to warrant thorough examination.

Accordingly, in 1947 the Institute appropriated the sum of $30,000 and obtained a grant of like amount from the Rockefeller Foundation to sponsor a study of business income. George O. May was the moving spirit in the organization of a study group. The chairman was Percival F. Brundage, senior partner of Price Waterhouse & Co., who served as president of the Institute in 1948-49, succeeding Mr. Bailey. Mr. May

was named research consultant of the group. The deliberations of the study group occupied about five years. Its report was published by the Macmillan Company in 1952 in book form. Some 40 to 50 persons participated in the deliberations. There was an executive committee of six, consisting of Mr. Brundage as chairman; Arthur H. Dean, a prominent lawyer; Solomon Fabricant, a prominent economist; Chester I. Barnard, a prominent industrialist; and two other certified public accountants, George D. Bailey and Samuel J. Broad. Other CPAs who participated in the group's deliberations were T. Coleman Andrews, Carman G. Blough, James L. Dohr, Stephen Gilman, Howard C. Greer, Alvin R. Jennings, Hiram T. Scovill, J. Harold Stewart, William W. Werntz, Edward B. Wilcox, and Robert T. Briggs. Representatives of the New York Stock Exchange, the SEC and other government agencies, as well as economists, businessmen, and lawyers constituted the remainder of the group.

The major thrust of the report was that corporations whose ownership was widely distributed should be encouraged to furnish information that would facilitate the determination of income measured in units of approximately equal purchasing power. This, in effect, was advocacy of price-level accounting. Among those dissenting to this approach was, significantly, Earle C. King, chief accountant of the SEC. Other dissenters were Messrs. Bailey, Blough, Werntz and Wilcox, and Charles W. Smith of the Federal Power Commission.

The discussion in the report was generally conceded to be of great value in bringing diverse minds to bear on the problem of defining business income and in reaching some areas of agreement, as well as in providing a basis for further studies. However, the report did not bring about any immediate change in accounting practice.

Meanwhile, the Institute, by means of a questionnaire, sought opinions on price-level accounting of several hundred prominent business executives, economists, investment analysts, and others. The responses showed wide diversity of views, but a substantial negative attitude.

In 1947, the committee on accounting procedure, after considering the available evidence, issued Accounting Research Bulletin No. 33, entitled "Depreciation and High Costs." It concluded that a basic change in accounting treatment to reflect changes in the purchasing power of the currency would confuse readers of financial statements, but that the committee would support the use of supplementary schedules, explanations, or footnotes by which the need for the retention of earnings to replace fixed assets would be made clear. For the time being, though not forever, as will be seen in a later chapter, the subject of price-level accounting was tabled.

Pressure From Academia

The tentative statement of accounting principles issued by the American Accounting Association in 1936, and the 1941 revision, omitting the word "tentative"—which deletion was noted with approval by the SEC's chief accountant—also put pressure on the Institute indirectly.

At first, the Association's emphasis was not on comparability of net income specifically, but rather on the need for a comprehensive, consistent framework of basic principles by reference to which specific questions of accounting procedure could be settled as they arose.

Individual accounting professors criticized the Institute's "common-law" approach to the solution of specific problems, without reference to a basic theoretical foundation. The editor of the *Accounting Review* even accused the committee on accounting procedure of rationalization, in its early bulletins, to support practices already followed by accounting firms. The fact that some of the Accounting Research Bulletins approved alternative procedures which could not be reconciled from a theoretical viewpoint also drew fire from some academicians.

In 1948 and 1957, the American Accounting Association again revised its basic statement on accounting principles. The

1948 revision was entitled "Accounting Concepts and Standards Underlying Corporate Financial Statements." The 1957 revision was entitled "Accounting and Reporting Standards for Corporate Financial Statements."

The 1957 revision included a final paragraph on comparability, which stated in part:

> Because the effective use of financial statements involves interperiod and intercompany comparisons, comparability of data over time and among companies is important. The principal barriers to such comparability are distortions resulting from price fluctuations and variations in accounting methods.

As to price-level changes, the statement recommended that supplementary data be furnished investors that would help them in evaluating the significance of price fluctuations—at least until reasonably uniform principles of adjustment for price changes were commonly accepted.

On variations of accounting methods the statement said, "Uniformity of accounting method is neither expected nor necessarily desirable, but reasonable comparability of reported data is essential. . . . When alternative practices in common use give materially different results, the practice adopted should be stated and the data required to achieve reasonable comparability should be supplied."

These statements, and the discussion they engendered, could not be ignored.

Pressure From Analysts

As the number of investors increased, the need for expert investment analysis and advice became more urgent. In response, a group known as financial analysts emerged. For the most part, they were employed by commercial and investment bankers, stock-brokerage firms, and investment advisory services, although some analysts served as independent consultants.

At first, most analysts were in the financial centers of New York and Boston, and local societies were formed there. But soon the numbers increased and other local societies were formed in various parts of the country. By 1947, it was considered desirable to form the Financial Analysts Federation, which, as the name suggests, was a national organization of constituent local groups, not of individuals.

There were no standards of qualification for financial analysts, and the somewhat loose, federation-type organization offered little promise of establishing such standards. Accordingly, under the auspices of the Federation, an Institute of Chartered Financial Analysts was organized. After conferring with the American Institute to learn how the Uniform CPA Examination was administered, the Institute of Chartered Financial Analysts set up a program of examinations and preliminary requirements. Those who met the requirements and passed the examinations, which included accounting subject matter, were authorized to use the title "Chartered Financial Analyst."

The financial analysts were, naturally, keenly interested in improving corporate financial reports. In their meetings and publications, they called for more and better information. Since advising choices among investments was their stock in trade, they reacted favorably to the growing demands for accounting principles which would facilitate comparability of earnings per share.

By establishing formal co-operative relations with the SEC and the American Institute, the financial analysts added their friendly influence to the forces which were pressing for action in this direction.

Pressure From the Press

Financial writers were beginning to publish stories, some of them sensational, on accounting procedures which, in their

view, failed to provide reliable information. One headline read: "Phantom Profits Worry Foresighted Managements."

"These articles," said Earle King in a 1948 speech, "and the language in which they are written, have an inevitable tendency to discredit generally accepted accounting procedures, the good faith of responsible corporate officials, the competence of the independent accountants, and the safeguards afforded by a Securities Act which outlaws misleading financial statements. Briefly, if the financial statements now in current use present a false picture, we must re-examine our principles."

Yet, in 1949, an article in a well-known financial weekly bore the heading, "Too Many Annual Reports Still Are Guessing Games."

The journalistic hunt was on. The press was becoming aware that controversy over accounting principles made news of interest to the financial community. And the raw material of which such news could be made was soon forthcoming in the speeches of a prominent member of the accounting profession—to be described shortly.

Pressure From Within the Institute

A growing uneasiness developed within the Institute in the face of apparent dissatisfaction in various quarters with corporate financial statements audited by its members, despite the hard work and increasing influence of the committee on accounting procedure.

Maurice H. Stans, then a member of the committee on accounting procedure, who became president of the Institute in 1954, expressed concern about the situation in an article in *The Journal of Accountancy* in December 1949. He wrote:

> . . . it is important that we examine critically into the reasons why corporate financial statements of today meet with such cynicism and distrust. What is wrong with accounting as the public sees it? Could

> it be the fact that there is still no broad authoritative code of accounting principles? Could it be that the two principal accounting organizations in the country take opposite positions on many basic issues? . . . Could it be that there are still no fixed standards of minimum disclosure for financial statements? Could it be that there is a great variety of form and content in financial statements, making it difficult to compare one company with another?

Similar questions were raised by other CPAs, but for some years the discussions were kept within the bosom of the family. Then, suddenly, the issues were thrust into the public domain.

In March of 1956, some members of the accounting profession were mildly stirred by a speech by Leonard Spacek, managing partner of Arthur Andersen & Co., before the Financial Analysts of Philadelphia.

The main theme of this speech was that depreciation provisions should be adjusted to reflect decline in the purchasing power of the dollar. This was a legitimate argument. George O. May and many others had advocated the same change in accounting. What irritated some of Mr. Spacek's colleagues were his remarks about the profession itself.

> There are many people in the accounting profession who feel that their obligation is fulfilled by reporting the figures and amounts taken from the records of the company. . . . You may have heard the assertion that income statements prepared in this manner conform to the "generally accepted accounting principles" currently prevailing as the policy of the American Institute of Accountants. Let me assure you that it has not become heresy to raise the question, "What are generally accepted accounting principles?" . . . Nor, in my view, can an accountant excuse himself or his actions by seeking cover in the shadow of a phrase which cannot stand re-examination in the light of day.

The press happily reported this speech.

A little more than a month later, Mr. Spacek extended the scope of his disapproval in an address before the local branch of the Controllers Institute of America in Chicago, entitled "Accounting Has Failed to Prevent Major Misrepresenta-

tions." He referred to "antiquated accounting principles," applied to new facts and in the context of current business realities. He compared members of the accounting profession who reported history alone to coroners in the medical profession.

Besides advocating depreciation provisions giving effect to decline in the purchasing power of money, he declared that accounting principles had failed to make financial statements informative where federal tax provisions were not related to the income currently reported: "Borrowing tax deductions from the future to reduce present federal income taxes represents an overstatement of present income." He then said that there had been failure to recognize the true financial significance of long-term leases of certain types of property—often motivated by a desire to avoid showing a liability for debt on the balance sheet. He concluded, "The accounting profession has not yet matured to the point where it draws its principles of accountability from a judicial consideration of the pros and cons of each issue."

This speech received even wider publicity than its predecessor.

A few months later, in October 1956, Mr. Spacek spoke before a commerce and industry luncheon in Chicago. Some of the barbs in this address were the following:

> I would like to tell you that our profession is standing steadfast to our principles and responsibilities. This I cannot do. . . . I find that the most serious problems of our profession are caused by our own indulgence . . . proper accounting has never in any notable way been the subject of advance planning by the profession or the public. . . . We must wait for the catastrophe, because we do not have a sufficiently strong or self-appraising accounting profession to right this public wrong—before, not after, serious injury results.

As illustrations of the application of accounting principles which produced results "out of balance with honest accountability" he referred to accelerated depreciation for tax pur-

poses, stock options, lease-backs, and the effect of inflation on reported profits.

He concluded that the accounting profession presently did not have a means of solving these problems: the group before which the problems were brought had no authority, and no accountant was required to observe its conclusions; its members consisted primarily of practicing members of the profession who in most cases should be disqualified because they were interested parties; the profession had not developed standards of accountability from which accounting principles must be derived; and the arguments for and against any position were not made or answered in public. He proposed a court of accounting principles whose members were not affiliated with the accounting profession and whose decisions would be mandatory for the entire profession.

In August 1957, Mr. Spacek elaborated this proposal for an accounting court before the American Accounting Association. He asked what basis there was for alternative accounting practices for the same transaction, even though the alternatives fell within the loose framework of so-called "accepted accounting principles." Comparison of earnings with those of other companies he considered a "dominant factor." He contended that the presence of alternative principles tended to eliminate the preferable principles in favor of those less desirable. He recommended an accounting court to establish accounting principles and outlined a possible structure for such a tribunal.

By this time many practicing CPAs were deeply disturbed. While recognizing Mr. Spacek's right to express his views on specific technical questions, many of his colleagues resented the free-swinging manner in which he attacked the accounting profession as a whole.

The newspapers were gleefully quoting his colorful phrases, and it was feared that the result might be a loss of confidence in corporate reports, which were actually getting better than they had been—largely due to the hard work of the committee on accounting procedure.

The climax of the first phase of Mr. Spacek's campaign for "comparability" was an address before the Milwaukee Control of the Controllers Institute, in which he acknowledged critical comments from his fellow accountants and others on speeches he had been making in recent months. He replied with relish to the criticisms. "There is only one reason for misleading financial statements. It is the failure or the unwillingness of the public accounting profession to square its so-called principles of accounting with its professional responsibility to the public." He quoted Oswald W. Knauth, former treasurer of R. H. Macy & Co. and professor at Columbia and Princeton, as follows: "Comparisons between two companies in the same industry, and to a greater extent between two companies in different industries and between entire industries, are so arbitrary as to be not only worthless, but dangerous."

Mr. Spacek then flung down the gauntlet. He accused the committee on accounting procedure of yielding to industry pressure on an important principle without public discussion. He criticized the committee also for failing to issue bulletins in the face of substantial internal dissent. Finally he impugned the motives of members of a special committee of the Institute appointed to investigate and report on divergencies between generally accepted principles of accounting and the accounting practices prescribed for railroads by the Interstate Commerce Commission.

A wave of indignation greeted this speech.

Marquis G. Eaton, then president of the Institute, was authorized by the executive committee to appoint a special committee to investigate these charges, consisting of Maurice E. Peloubet, J. S. Seidman, and L. H. Penney, chairman. This committee made a thorough investigation, which included a meeting with Mr. Spacek, a questionnaire to the members of the committee on accounting procedure, a review of the proceedings of the committee, and personal discussions with the chairman of the committee on relations with the Interstate Commerce Commission. Under date of April 17, 1957, this

committee submitted a 33-page report to the Council with the following conclusion:

> We do not find that there was any yielding to improper influences by the committee on accounting procedure or the committee on relations with the Interstate Commerce Commission. We do find that the viewpoint of oil industry representatives in the case of the committee on accounting procedure, and a railroad representative in the case of the committee on relations with the Interstate Commerce Commission, was obtained. We find that there was nothing improper about the obtainment of such viewpoint. We find that the obtainment of such a viewpoint did not frustrate or impair consideration on their merits of the technical subjects involved.

President Eaton thought something affirmative ought to be done about the unfavorable publicity the profession was receiving. He was a partner of the firm of Eaton & Huddle of San Antonio, Texas, and a man of unusual leadership capacity. He decided that as president of the Institute he should respond to the criticisms which had been voiced.

An invitation to speak to the Illinois Society of Certified Public Accountants provided an opportunity to make such a statement. The title of his address was, "Financial Reporting in a Changing Society." Some 50,000 reprints were sent to presidents of listed companies, bankers, economists, educators, business leaders, government officials, labor leaders and others. After discussing the changing nature of the economy and the importance of profit determination, Mr. Eaton said:

> There is some reason to believe that this phrase—"generally accepted accounting principles"—suggests to the ordinary reader the existence of some authoritative code of accounting, which when applied consistently will produce precise and comparable results. The appearance of precision is strengthened by the reporting of net income in exact dollars and cents, instead of rounded approximations.
>
> Now, we accountants all know that "generally accepted accounting principles" are far from being a clearly defined, comprehensive set of rules which will insure the identical accounting treatment of the same kind of transaction in every case in which it occurs. We know that "generally accepted accounting principles" are broad con-

> cepts, evolving from the actual practices of business enterprises, and reflected in the literature of the accounting profession. To be sure, many of these principles have been formally defined or clarified in the Accounting Research Bulletins of the American Institute. But we all know that in some areas there are equally acceptable alternative principles or procedures for the accounting treatment of identical items, one of which might result in an amount of net income reported in any one year widely different from the amount an alternative procedure might produce.

He cited alternative methods of inventory pricing and depreciation as examples and continued, "Yet, I suspect it would come as something of a shock to some people to realize that two otherwise identical corporations might report net income differing by millions of dollars simply because they followed different accounting methods—and that the financial statements of both companies might still carry a certified public accountant's opinion stating that the reports fairly presented the results in accordance with 'generally accepted accounting principles.' "

Mr. Eaton mentioned the existing requirement of consistency in the determination of income of a single company from year to year, and went on to say, "Perhaps comparability among companies and industries is unattainable—perhaps it is not even desirable. . . . In any event, the question whether comparability in financial reports among companies and industries is the ultimate objective—and whether it is obtainable—is fundamental to our problem. It seems to me that the accounting profession should have the help of the business and financial community in answering it."

Mr. Eaton affirmed the willingness of CPAs to assume responsibility for their own opinions, but said that no one could understand the significance of generally accepted accounting principles without realizing that like the common law they developed by the evolutionary process and that their development would probably never be completed.

He concluded by stating that while the Institute had accepted the responsibility for leadership in the insistent search

for better methods of financial reporting it could not assume the sole responsibility for the result. Corporation managements, he said, had the primary responsibility for their own statements; government also shared responsibility; and bankers, financial analysts, and others had some responsibility to advise how financial statements might be made more useful for the purposes they were intended to serve.

This address was intended to be a statement of position, a candid acknowledgment of the limitations of accounting, and an invitation to interested members of the public to co-operate in the Institute's efforts.

Immediate reactions were encouraging.

The president of the New York Stock Exchange wrote:

> . . . it is the consensus of opinion that this is one of the most lucid statements on the subject that we have seen . . . While the content of financial statements is primarily the responsibility of the companies involved—we believe that the accountng profession will be doing a service both to itself and the investing public by championing more adequate and, to the extent possible, more uniform and comparable reporting.

The research director of a large labor union wrote that the statement was "most welcome."

The president of a small bank wrote, "We are so impressed with the booklet that we would like to distribute a copy to our staff. . . ."

Scores of additional letters were received. But while the speech clarified the problem, and the profession's difficulties in coping with it, the solution remained as remote as ever. There were no volunteers to help the accountants pull their chestnuts out of the fire.

Countervailing Pressure

While pressure for reasonable comparability of earnings came from the SEC, the universities, the analysts, the press, and from within the profession itself, a strong, though not so

visible, countervailing pressure was persistently exercised by some corporate managements.

It was not that these managements were against comparability. They simply were against relinquishing their right to present their financial statements in accordance with accounting principles which had stood the test of time and, as they saw it, were best suited to the peculiar nature of their businesses.

Yet, whenever the committee on accounting procedure proposed elimination of some alternative procedure theretofore permissible, some companies were threatened with the necessity of changing customary methods—and they often resisted. Their resistance might be manifested directly, or through the Controllers Institute, the Edison Electric Institute, or other trade organizations.

After all, the SEC had stated officially that management had primary responsibility for its financial statements. What authority did auditors have to dictate to management the accounting methods it must follow? So long as such methods had substantial authoritative support, why should auditors hesitate to give a clean opinion on the financial statements?

Furthermore, corporate managements were developing a greater interest in the market price of their common stocks than ever before. There were several reasons for this. Stock options to executives gave them immediate personal interest in the reported earnings of their companies. The continual need for new capital made it obviously desirable to keep the market price of a company's stock as high as possible, and this depended on reported earnings. Also, acquisitions of other companies through exchanges of stock often seemed more desirable than outright purchases. The higher the market value of the acquiring company's stock, the more advantageous the acquisition.

In these circumstances it was to be expected that any change in accounting principles that would result in reducing reported earnings of a substantial number of companies would be resisted with vigor.

The large corporations were not without resources and

influence. They had access to the SEC, the stock exchanges, and the press. In one dramatic episode, indeed, resort was had to the courts.

The right of the Institute's committee on accounting procedure to issue opinions on preferred methods of financial reporting was challenged by a group of public-utility companies in 1959.

The committee was proposing to issue a letter interpreting the phrase "a deferred tax account" in Accounting Research Bulletin No. 44 (Revised), "Declining-balance Depreciation." The letter said:

> The committee used the phrase in its ordinary connotation of an account to be shown in the balance sheet as a liability or a deferred credit. A provision in recognition of the deferral of income taxes, being required for the proper determination of net income, should not at the same time result in a credit to earned surplus or to any other account included in the stockholders' equity section of the balance sheet.

A group of utility companies obtained a temporary injunction against the Institute, in a United States District Court, preventing the issuance of this letter. The companies contended that the issuance of the letter would cause credit-granting agencies, financial analysts, and others to question their inclusion in the equity sections of their balance sheets of amounts shown as "earned income taxes," and that this might impair their borrowing power and otherwise damage them. They alleged that in preparing to issue the interpretive letter the Institute's committee had not gone through the usual exposure processes required by its own rules prior to the issuance of Accounting Research Bulletins.

The executive committee of the Institute considered this situation at great length. Some members of the committee were inclined to try to work out some compromise with the utility companies to avoid a fight in court. The majority felt, however, that the power of the committee on accounting procedure to issue Accounting Research Bulletins might be curtailed if the

Institute avoided the confrontation. The precedent might tempt other powerful corporations to take legal action whenever the committee was about to issue a bulletin of which they disapproved. The final decision was to fight the matter out with the utility companies, no matter what the cost.

A hearing was held early in May before a judge of the District Court who held that "the purposes of the defendant Institute are adequate justification, if justification indeed be required, to permit the proposed communications."

However, the judge issued a temporary injunction enjoining the mailing of the interpretive letter pending a further hearing by the Court of Appeals on a motion to be made in that court for an injunction.

The Court of Appeals, in a unanimous opinion, upheld the decision of the District Court, saying:

> We think the courts may not dictate or control the procedures by which a private organization expresses its honestly held views. Defendant's action involves no breach of duty owed by them to the plaintiffs. On the contrary, every professional body accepts a public obligation for unfettered expression of views and loses all right to professional consideration, as well as all utility, if its views are controlled by other criteria than the intellectual conclusions of the person acting. Absent of showing of actual malice or its equivalent, the courts would be making a great mistake, contrary indeed to their own ideas and professions, if they assumed to restrict and denigrate this widely recognized and assumed professional duty.

However, the Court of Appeals reinstated the injunction pending a hearing by a justice of the United States Supreme Court on an application for further injunction. This application was heard and denied by a justice of the Supreme Court in July, who said that "in my judgment none of the questions proposed to be presented in the petition for certiorari have the prospect of commanding four votes for review."

Thus, at considerable expense, the Institute asserted and successfully defended its right to issue opinions on accounting principles.

Yet frequent objections by corporate managements to pro-

posed accounting changes could not be ignored by the committee on accounting procedure, and it necessarily approached each problem with caution and deliberation. Nevertheless, it had been far from unproductive during these hectic years.

The Committee on Accounting Procedure

The mission of the committee on accounting procedure might have been described in 1939 as that of bringing order out of chaos. Its members struggled manfully to deal with the multitude of questions raised by the SEC and others to which no authoritative answers had, as yet, been provided.

The transition of the national economy from a defense program to a full war basis in 1941 gave rise to a multitude of difficult accounting problems which had to be dealt with at a time when numerous additional pressing demands were being made for the services of accountants. Walter A. Staub, who succeeded George May as active head of the committee, carried the burden during those war years.

Mr. Staub was a senior partner of Lybrand, Ross Bros. & Montgomery. He was a man of strong character and absolute integrity, highly disciplined, and probably one of the ablest technicians and hardest working members that the profession had produced.

It was apparent that war conditions had greatly accentuated the tentative character of corporate financial statements. Reserves were being created for various purposes, including possible postwar developments. Renegotiation of war contracts introduced an additional element of uncertainty in the reporting of current profits. Later the termination of war contracts raised similar problems. Accounting for income and excess-profits taxes involved difficult questions, as did accounting for fully amortized emergency facilities and for the recovery of war losses.

At the same time the SEC was raising basic questions which required attention, such as the propriety of charges to surplus,

the write-off of intangibles, quasi-reorganizations, and other matters which the committee could not ignore.

Also the committee's attention was frequently distracted to specific problems such as accounting for regulated industries, notably public utilities, and financial reports required by the Office of Price Administration.

A rapid turnover in its research staff greatly added to the burdens on the members of the committee. In addition, they were subject to many pressures. From time to time the SEC disagreed with the committee's views on specific problems. Occasionally members of the Institute, voicing disapproval through state society organizations, disagreed with the committee's findings. The corporations whose statements were affected by the committee's decisions also had to have their say. In the circumstances the committee deserved much credit for maintaining a high level of productivity in an extremely difficult period.

After the war the committee reported with satisfaction the engagement of Carman G. Blough as full-time director of research and of Paul L. Graber of Tulsa University, Oklahoma, as research assistant.

It was stated that the committee would hold at least four meetings a year, and would experiment with two-day meetings beginning at its next session. This report concluded with the statement, "Right now there are more problems than time, but progress is being made on many important problems."

Between 1945 and 1953, the committee issued the following Accounting Research Bulletins:

- ARB No. 26 Accounting for the Use of Special War Reserves
- ARB No. 27 Emergency Facilities
- ARB No. 28 Accounting Treatment of General Purpose Contingency Reserves
- ARB No. 29 Inventory Pricing
- ARB No. 30 Current Assets and Current Liabilities—Working Capital
- ARB No. 31 Inventory Reserves

ARB No. 32	Income and Earned Surplus
ARB No. 33	Depreciation and High Costs
ARB No. 34	Recommendation of Committee on Terminology—Use of Term "Reserve"
ARB No. 35	Presentation of Income and Earned Surplus
ARB No. 36	Pension Plans—Accounting for Annuity Costs Based on Past Services
ARB No. 37	Accounting for Compensation in the Form of Stock Options
ARB No. 38	Disclosure of Long-term Leases in Financial Statements of Lessees
ARB No. 39	Recommendation of Subcommittee on Terminology—Discontinuance of the Use of the Term "Surplus"
ARB No. 40	Business Combinations
ARB No. 41	Presentation of Income and Earned Surplus
ARB No. 42	Emergency Facilities—Depreciation, Amortization, and Income Taxes

In spite of all its difficulties, the committee on accounting procedure was making a strong impression in the financial community. Gradually its recommendations were being implemented in the published reports of prominent corporations. The increasing visibility of the profession, largely as a result of the committee's work, was reflected in an address by James J. Caffrey, then chairman of the Securities and Exchange Commission, at the Institute's 1947 annual meeting. He said, "History has thus thrust the accountant into a crucial role . . . the accountant is no mere reporter. . . . Save in the simplest kinds of business, he has been given a task which embraces interpretation as well as mere recording. . . . Perhaps the simplest way of putting it is to say that the accountant's position has become a position of power. In this regard history has an even hand; with power she doles out responsibility."

In a 1947 report the committee on accounting procedure said, "Looking back over the bulletins that have been issued, it is comforting to find that they have been pretty well accepted. Their use seems to be growing in those areas in which

there were violent differences of opinion at the time of issuance."

While the committee had assumed a leading role, and was making progress, there were several basic weaknesses in its operation. First of all, it had inadequate staff help. While the accession of Carman Blough had greatly facilitated the work, the research assistants which he had engaged were also trying to help the committee on auditing procedure and other technical committees. The resources of the Institute were still limited, and it was receiving no outside financial support.

Carman Blough, in addition, was in constant demand as a speaker at meetings of state societies and other accounting groups. He was in a position to keep the profession, as well as the industrial accountants, fully informed of the thinking of the committees on accounting and auditing procedure, and the problems which they had under consideration. This was important. Only if the profession as a whole and business management were well informed, could the committee hope to have effective support in eliminating accounting practices which had previously been accepted, in order to narrow the areas of difference. Mr. Blough's appearances as spokesman for the Institute on technical matters had a profound influence on practice throughout the country. The members respected him highly, and were generally inclined to "do what Carman Blough wants us to do."

The result, however, was that much of the work of the committee on accounting procedure had to be done by volunteers—all busy men. The pace of progress, therefore, became somewhat erratic. Many of the committee's conclusions were not supported by research in depth. If a two-thirds majority for a proposal could not be mustered, a problem might be tabled indefinitely.

Finally, the Accounting Research Bulletins had no teeth in them. It had been decided at the outset that the bulletins' authority should depend on general acceptability, and that the burden of proof should be on the accountant who departed

from the conclusions. Each bulletin carried a footnote to this effect.

Many of the bulletins were phrased in such a way as to leave room for exceptions in special circumstances, and to stress the necessity for professional judgment in their application. As a consequence, except as the SEC or the New York Stock Exchange insisted on compliance, individual companies and auditors were at liberty to deviate if they chose to assume the burden of justifying their departure.

With the support of the SEC, however, the committee did eradicate many undesirable practices. Most of the questionable practices in evidence in 1938 had completely disappeared by the early 1950's.

Yet the committee hesitated on some occasions to make firm choices among alternative procedures and was reluctant to condemn widely used methods even though they were in conflict with its preferences.

Differences of opinion within the profession undoubtedly had made it more difficult to reach firm, clear-cut conclusions. Some of these differences occurred because the various parties to the discussion were proceeding from different theoretical assumptions. Some of the differences arose from differing philosophies. These divergent philosophical positions have been described in over-simplified terms in the phrase "uniformity, flexibility and comparability."

Carman Blough stated the situation accurately:

> Some seem to believe that uniformity of accounting principles and procedures is what is most needed; that rules should be established in such detail that similar transactions would always be handled similarly in the accounts. Comparability is their goal. Others believe that such uniformity would be impossible, but firmly believe that much more uniformity than we now have would not only be possible but highly desirable. Still others consider uniformity to be highly dangerous. To them, subjective judgment in each case should govern; they believe consistency, accompanied by disclosure, is of primary importance.

In spite of everything, the committee's record was creditable, and its influence significant.

In 1952, it produced a restatement and revision of the 42 bulletins previously issued, under the designation Accounting Research Bulletin No. 43.

In the next six years it published the following:

ARB No. 44	Declining-balance Depreciation (Revised)
ARB No. 45	Long-term Construction Type Contracts
ARB No. 46	Discontinuance of Dating Earned Surplus
ARB No. 47	Accounting for Costs of Pension Plans
ARB No. 48	Business Combinations
ARB No. 49	Earnings Per Share
ARB No. 50	Contingencies
ARB No. 51	Consolidated Financial Statements

In the fall of 1959, the committee submitted its final report, which was presented to the Council by its chairman, William W. Werntz.

"Throughout the history of the committee," this report said, "its bulletins have increasingly been recognized as authoritative by the profession, by the business world, by governmental agencies and by the courts." It noted that 124 members of the Institute had served on the committee since its inception. The list included many of the most distinguished members of the profession, both from the practicing and academic branches.

The torch laid aside by the committee on accounting procedure was picked up in 1959 by the newly created Accounting Principles Board, the genesis of which will be described in the next chapter.

CHAPTER 5

Time for a Change – The APB

At the 1957 annual meeting, Alvin R. Jennings, then nominee for president of the American Institute, delivered an address entitled, "How Can CPAs Meet Present-Day Challenges of Financial Reporting?" Mr. Jennings had become the managing partner of Lybrand, Ross Bros. & Montgomery. For many years he had been active in the affairs of the Institute and other professional organizations. He was widely regarded as a thoughtful and articulate man of unquestioned integrity and courage. In the light of the events described in the preceding chapter, his address was listened to with unusual interest.

"There are few, if any, undertakings in which the process of self-examination is not helpful," Mr. Jennings said.

He reviewed the history of the efforts to develop generally accepted accounting principles, from the time of the correspondence with the New York Stock Exchange, published in 1934, to the time when he spoke. He praised the work of the committee on accounting procedure, but expressed some regret at its failure to enlist the active co-operation of in-

dustry spokesmen: "The fault is not altogether ours—in fact, I think it rests largely upon a failure of industry to acknowledge in any major sense its own obligations, and a disposition to interpret leadership by the Institute as an indication of willingness to assume full accountability."

Mr. Jennings advocated heavier emphasis on accounting research:

> In the field of medicine pure research is largely in the hands of biochemists and other specialists, and not in the normal province of the practicing physician. Techniques exist to test new drugs before they are offered to the public. In law, the continued acceptability of established concepts is tested each time a case goes to trial. We have no comparable laboratory in which the new may be examined and tested against the old. This is a serious handicap to creative thinking.

He suggested that development of accounting principles should be regarded as in the nature of pure research; that an adequate research organization should be provided; that this research organization should be composed in part of staff whose background would enable them to contribute the academic and industrial points of view; that industry and the accounting profession should share the cost of the program; that the research organization should carry on continuous examination of basic accounting assumptions, and develop authoritative statements for the guidance of both industry and the accounting profession; that statements issued by the research organization should be submitted to the Council of the Institute for approval or rejection of the conclusions; and that upon receiving approval of two-thirds of the members of Council any such statement should be considered binding upon members of the Institute.

Mr. Jennings pointed out that research was a full-time job and should be recognized as such. He questioned whether a committee of volunteers could move fast enough to keep up with economic and social changes affecting accounting and financial reporting.

Referring to the invaluable assistance of Carman Blough,

soon to retire as director of research, Mr. Jennings said, "It will not be easy, if in fact it is possible, for us to find five or six Carman Bloughs. Yet I am convinced that is what is needed, and we must set about it and do the best we can."

Mr. Jennings concluded his address by reaffirming faith in the concept of generally accepted accounting principles as necessary to an objective determination of the fairness of financial representations. He urged the accounting profession to accept its fair share of responsibility for the identification of those principles, but to take into partnership others whose roles in the economy invested them with parallel interests in this process. He asserted that accounting principles must be sufficiently rigid to give meaning to financial reporting, but sufficiently flexible to permit change when circumstances required. Finally, he urged increased efforts to educate the interested public as to the nature and unavoidable limitations of financial statements.

A Fresh Start

This speech called for a new approach and a fresh start. The profession was ready for it. A special committee on research program was appointed, the chairman of which was Weldon Powell, one of the senior partners of Haskins & Sells and an acknowledged authority on accounting theory. Other members were Andrew Barr, who had succeeded Earle King as chief accountant of the SEC; Carman Blough, former chief accountant of the SEC and then the Institute's research director; Dudley E. Browne, a past president of the Controllers Institute of America, and controller of the Lockheed Corporation; Arthur M. Cannon, professor at the University of Washington; Paul Grady, a distinguished partner of Price Waterhouse & Co.; Robert K. Mautz, of the University of Illinois; Leonard Spacek, senior partner of Arthur Andersen

& Co., whose interest in the subject had been clearly shown by his speeches; and William W. Werntz, former chief accountant of the SEC and at that time a partner of Touche, Ross, Bailey & Smart.

This high-powered committee went to work immediately, and by intensive effort was able to submit recommendations in September 1958, only 11 months after Mr. Jennings' address.

First, its report set forth some basic considerations:

> The general purpose of the Institute in the field of financial accounting should be to advance the written expression of what constitutes generally accepted accounting principles, for the guidance of its members and of others. This means something more than a survey of existing practice. It means continuing effort to determine appropriate practice, and to narrow the areas of difference and inconsistency in practice. In accomplishing this, reliance should be placed on persuasion rather than on compulsion. The Institute, however, can, and it should, take definite steps to lead in the thinking on unsettled and controversial issues.
>
> The broad problem of financial accounting should be visualized as requiring attention at four levels: first, postulates; second, principles; third, rules or other guides for the application of principles in specific situations; and four, research.
>
> Postulates are few in number and are the basic assumptions on which principles rest. They necessarily are derived from the economic and political environment, and from the modes of thought and customs of all segments of the business community. . . . A fairly broad set of co-ordinated accounting principles should be formulated on the basis of postulates. . . . The principles together with the postulates should serve as a framework of reference for the solution of detailed problems.
>
> Rules or other guides for the application of accounting principles in specific situations, then, should be developed in relation to the postulates and principles previously expressed. Statements of these probably should be comparable as to subject matter with the present Accounting Research Bulletins. They should have reasonable flexibility.
>
> Adequate accounting research is necessary in all of the foregoing. Pronouncements on accounting matters should be based on thoroughgoing independent study of the matters in question, during which

> consideration is given to all points of view. For this an adequate staff is necessary. . . . Research reports or studies should be carefully reasoned and fully documented. They should have wide exposure to both the profession and the public.

The report emphasized the necessity for close co-operation with industry, governmental agencies, stock exchanges and other professions.

The committee proposed a dual organization for carrying out the program, consisting of an Accounting Principles Board and an accounting research division, whose director would be responsible for carrying out the research program, with the assistance of a technical staff.

Accounting Research Studies would be published, presenting detailed documentation and pro-and-con arguments on controversial points, with conclusions or recommendations, and illustrations of the application of principles. Immediate projects of the accounting research staff were to be a study of the basic postulates underlying accounting principles, and a study of the broad principles of accounting. Project advisory committees would work with the accounting research staff on each project.

Statements on generally accepted accounting principles would be issued by the Board and would be expected to be regarded as authoritative written expressions of what constituted generally accepted accounting principles. Ordinarily, they would be based on Accounting Research Studies.

Statements on generally accepted accounting principles would not be presented to the Council or to the membership of the Institute for approval except in rare cases.

The Accounting Principles Board would, of course, supersede the existing committees on accounting procedure and terminology. Previously issued Accounting Research Bulletins would be continued in force with the same degree of authority as before, unless and until the Board reviewed or revised any of them.

A detailed plan of organization and procedure was presented with the report.

The Council of the Institute approved with enthusiasm these

proposals of the distinguished committee. The program was embodied in a formal resolution of the Council known as the "charter" of the Accounting Principles Board. Mr. Powell, chairman of the special committee, was elected the first chairman of the Board.

The new program did not take precisely the form recommended by Alvin Jennings in his 1957 speech. He had proposed a quasi-independent research establishment, manned by full-time accountants of high capacity—"six Carman Bloughs"—and representing the viewpoints of practitioners, academicians, and industrial accountants. As he conceived it, this research establishment would be authorized to publish studies for the guidance of the profession and the financial community. It would submit recommendations regarding accounting principles to the Council of the Institute, and if these recommendations were approved by two-thirds of the Council, they would become binding on all the members. The Council would not become involved in the details of the recommendations, but would concern itself only with the broad principles and objectives.

The new plan did result in the establishment of a semi-autonomous research division, headed by a director who had authority to publish research studies. The division had a much larger budget than had been available before, and accordingly a much larger staff. It was exclusively devoted to the development of accounting principles, and had no responsibilities to the technical committees of the Institute. This much was new.

The Accounting Principles Board itself, however, was not much different from the committee on accounting procedure which it succeeded. To be sure, Council had approved a more elaborate set of rules governing the Board's procedures. Also an innovation was the assumption that the Board would usually await the production of research studies before it made specific recommendations on a given subject.

However, like the committee on accounting procedure, the Council gave the Board authority to issue Opinions on its own

authority. Its rules required a two-thirds vote of its members before an Opinion could be issued. Dissents were to be published. Each of the Board's Opinions carried a note similar to that which appeared on the earlier Accounting Research Bulletins, to the effect that the authority of the Opinions rested on their general acceptability, and that while it was recognized that general rules might be subject to exception, the burden of justifying departures from the Board's recommendations must be assumed by those who adopted other practices.

The Board's membership, originally set at 18, was soon increased to 21 in order to distribute the workload more widely through subcommittees. The result was that no Opinion could be issued without the concurrence of 14 members. Thus, the Board was unable to avoid the difficulties involved in having 21 men sitting around a table, arguing about language as well as substance in drafts of proposed Opinions. The presumption that the Board would await production of a research study before addressing itself to a problem was also to lead to delays.

Financing the new research program was a subject of extended discussion in the executive committee. Initially it was decided to start the program with appropriations from the regular budget of the Institute, and this was done in the first year. As the costs grew heavier, however, it was decided to call on the members for contributions pledged over a five-year period. It was felt inadvisable to request contributions from industry, as Mr. Jennings had suggested. With little difficulty pledges amounting to about $875,000 were received from the membership, enough to support the program for a five-year period.

Dr. Maurice Moonitz, of the University of California, was engaged as director of research. He was recognized as an outstanding theorist of accounting. Dr. Perry Mason, a former president of the American Accounting Association, was designated as assistant director of research.

The two men began to recruit a research staff.

The first year of the Accounting Principles Board, 1959, was spent largely in getting organized. The research director, however, launched six important projects—on basic accounting postulates, broad accounting principles, income taxes, long-term leases, business combinations, and non-profit organizations. Contracts were made with university professors to conduct several of these studies. Project advisory committees were formed to consult with the researchers.

Dr. Moonitz and Dr. Mason addressed themselves to research with speed and vigor. A study on "The Basic Postulates of Accounting" by Moonitz was published in October 1961. In December of the same year, a study by Mason on "Cash-flow Analysis and the Funds Statement" was published.

In 1961 the Board reported that it had not yet reached a level of normal activity, since to a large extent its functions depended upon the completion of Accounting Research Studies by the research division.

The Board's first utterance was an interpretive Opinion in 1962 on new depreciation guidelines and rules issued by the Treasury Department.

A research study on pension plans was added to the agenda of the research division.

In May 1962, a study entitled "A Tentative Set of Broad Accounting Principles for Business Enterprises," by Professors Robert T. Sprouse and Moonitz, was published and widely distributed. This study, however, included strong dissents by a number of members of the project advisory committee.

Because of what were considered radical recommendations, which would require basic changes in currently accepted practices, the Accounting Principles Board refrained from endorsing this study. Nothing more was done for many years to implement the broad objective of establishing a framework of principles within which specific problems might be dealt with consistently.

The Investment Credit

Just as the Board was settling down to work under the new program and the research pipeline was being filled with studies in process, the Congress of the United States unwittingly precipitated one of the most heated controversies ever to take place within the accounting profession, and the most widespread public criticism of the profession since the McKesson case broke in 1938.

The Revenue Act of 1962 provided for an "investment credit"—a reduction of income tax—equal to a specified percentage of the cost of certain depreciable assets acquired and placed in service after 1961. The objective was to stimulate investment in productive assets, thus creating employment, increasing production, and sustaining the economic growth of the country.

The Accounting Principles Board was faced with the necessity of recommending appropriate accounting treatment of this new phenomenon. From the theoretical point of view, three concepts were possible: the credit could be considered a subsidy, by way of a contribution to capital; a reduction in taxes otherwise applicable to the income of the year in which the credit arose; or a reduction in the cost otherwise chargeable in a greater amount to future accounting periods.

There was no precedent to go by, and there was no time for research in depth, although the research division, under pressure, produced an unpublished memorandum in which it was concluded that the credit should be regarded as a reduction of taxes otherwise applicable to the income of the year. This was described as the "flow-through" method.

The members of the Accounting Principles Board split widely on the issue. One group took the position that net income should not be increased by investment in new facilities in a given year—it contended that the credit should be treated as a reduction of cost. Others argued that the credit was a reduction of taxes payable in a given year, and should be accounted for accordingly. In response to the counter-

argument that this could distort net income and thus impede comparability of earnings, it was asserted that many industries were continually expanding their plants, and that the credit would therefore be available year after year in any event. To treat each year's credits as reductions in the cost of assets, to be charged against income of future years, seemed unreasonable to proponents of this view.

At that time the Board included senior partners or managing partners of nine of the largest firms, three senior partners of large local firms, three financial executives of corporations (including one who had formerly been a professor of accounting), two eminent professors of accounting from large universities, the Comptroller General of the United States, and Carman Blough, who had retired as research director. It would have been difficult to assemble a more prestigious group.

It seemed essential to reach a conclusion by the end of 1962 in order that there might be some uniformity in approach in annual reports for that calendar year.

Since there was no precedent, no established practice for dealing with a tax credit of this nature, the situation offered an ideal opportunity to establish one practice, rather than alternatives which would obstruct efforts to compare the results of one company with those of another.

But the Board members were unable to agree. The argument became an angry one, and personal tensions developed.

Corporate managements did not hesitate to make their views known to the Board, to the SEC, and to their own auditors.

It was rumored that the Treasury Department was strongly opposed to any requirement that the investment credit be spread over a number of years: the basis of this opposition was believed to be a fear that the incentive to industry to acquire productive facilities would be diminished if the credit could not be reflected in profits for the year in which the investment was made.

Shortly before the Accounting Principles Board issued an Opinion on the question, but after the conflicting views among

its members had hardened, the chief accountant of the SEC wrote a letter to the Board expressing a preference for the flow-through method.

Finally, at a meeting early in December, a bare two-thirds majority of the Board was mustered in favor of spreading the investment credit over the productive life of the related asset. The majority was motivated mainly by the conviction that reported profits should not be increased by the purchase of productive facilities, and that only one way of accounting for the credit should be permitted, rather than alternatives which would impede comparability.

The majority's conclusion was stated in the Board's Opinion No. 2, which, while voted on in December, was not printed and distributed to members of the Institute until early in January.

Seven members of the Board dissented, and three of them announced that their firms would not follow Opinion No. 2, since they believed that they could assume the burden of justifying a departure. They expressed the belief that existing generally accepted accounting principles preponderantly supported the treatment of the investment credit as a reduction of current income taxes—the "flow-through" method.

The Opinion made an exception in the case of regulated industries, principally utilities, when regulatory agencies required different treatment for rate-making purposes from that recommended under generally accepted accounting principles.

The president of the Institute at this time was Robert E. Witschey, head of the local accounting firm of Witschey, Harman & White, in Charleston, West Virginia. President Witschey was greatly disturbed by the split within the Board and the implications for its work in the future. He was also concerned about the possibility that the Securities and Exchange Commission would not support the Board's conclusions in Opinion No. 2.

Accordingly a conference was arranged with the full Commission and its accounting staff late in December—after the Board had voted, but before the Opinion had been published.

The meeting was attended not only by Mr. Witschey, but by members of the Board representing both the majority and minority points of view.

Mr. Witschey made an opening statement, emphasizing the long-range implications of the decision which the SEC might make in this particular instance. He said, in part:

> From the beginning, the SEC has had the legal power to determine the accounting principles to be followed in financial statements filed with the Commission. . . .
>
> The Commission early decided that if the accounting profession, through the American Institute, would put out authoritative statements on accounting principles, the SEC would leave the initiative with the profession—always reserving the right, of course, to exercise its powers if the Institute's pronouncements were not acceptable to the Commission.

He said that this procedure had worked well and recalled that there had been only a few occasions on which the Commission had differed from the Institute's conclusions. He explained the reorganization of the Institute's research program and the objectives of the new Accounting Principles Board, including "continuing effort to . . . narrow the areas of difference and inconsistency in practice." In this effort, he said, the Institute had always had the encouragement of the SEC.

With specific reference to the investment credit, Mr. Witschey readily conceded that there were legitimate differences of opinion as to how it should be dealt with, but stated that the APB considered itself obliged to furnish guidance to its members. In reaching its conclusions, the Accounting Principles Board had followed its established procedures, including wide exposure of the draft Opinion with an opportunity for all interested parties to comment. He said that the Board had also carefully considered the letter of the Commission's chief accountant, indicating a preference for the so-called "flow-through treatment." He also summarized the views of the Board members in favor of one treatment or the other.

However, he emphasized that the majority felt that alternative methods should be discouraged, on the ground that they would increase the difficulty of making comparisons of earnings of different companies. He pointed out that it would have been much easier for the Board to say that in view of the novel character of the investment credit it could not object to any of two or more alternative treatments, but this would not have advanced the cause of narrowing the areas of difference and inconsistency in financial accounting practice.

He urged the Commission to support the Board's conclusion that the investment credit should be spread over the life of the related asset: "It should be helpful to you to have such a body [as the Accounting Principles Board] available to express its views on complicated technical questions with which you must deal. To the extent that you find its conclusions acceptable, the usefulness of the Board will increase, since there will be all the more respect for its Opinions. If the Commission permits alternative treatments, these difficulties may be increased."

Mr. Witschey concluded by stating that there were far more important questions of accounting principle to be dealt with in the months ahead than the investment credit, which happened to be at the moment a "hot potato" largely because of its immediate impact on current earnings of many companies.

"It would be very helpful in my opinion," said Mr. Witschey, "if at this particular juncture the good and courageous work that has been done by the Board should be found acceptable by your Commission. The psychological effect on the business and financial public would be good. The encouraging effect upon the Board itself would be good."

Following this statement members of the Commission and its staff questioned members of the Board who had accompanied Mr. Witschey, including the research director, and arguments for and against *Opinion* No. 2 were repeated. At the conclusion of the conference, the Commissioners promised to take the matter under advisement.

Under date of January 10, 1963, the Securities and Exchange Commission issued Accounting Series Release No. 96, "Accounting for the Investment Credit," which said, in part:

> In recognition of the substantial diversity of opinion which exists among responsible persons in the matter of accounting for the investment credit, the Commission will accept either a method which reflects the investment credit in income over the productive life of the acquired property, or a method which reflects 48 per cent of the investment credit (the maximum extent to which the credit can normally increase net income) in income as a reduction of the tax expense of the year in which the credit arises, and defers the balance of 52 per cent to subsequent accounting periods during which depreciation allowances for tax purposes are reduced because the statutory requirement reduces the basis of the property for tax purposes by the amount of the investment credit. The amount of such deferral should be segregated from taxes currently payable. The 100 per cent flow-through to income of the investment credit benefit in the year in which it arises will be accepted in the case of regulated industries when authorized or required by regulatory authorities. In all cases full disclosure of the method of accounting followed and amounts involved should be made where material.

The release also stated that, contrary to its usual policy, the SEC would accept qualifications in accountants' opinions, in cases in which departures from Opinion No. 2 made such qualifications necessary.

As it happened, most corporations chose to ignore the Board's Opinion No. 2, and to follow the alternatives permitted by the SEC. In many cases the amounts involved were considered immaterial in relation to total net income of the companies concerned. Neither the firms which agreed nor those which disagreed with the Board's Opinion took exceptions in cases where the flow-through method was used. Opinion No. 2 became a dead letter.

As a consequence, the Board threw in the sponge. In Opinion No. 4, issued in March 1964, Opinion No. 2 was amended by stating that either the spreading or the flow-through method of treating the investment credit was acceptable. Opinion No. 4

stated that the authority of Board Opinions rested upon their general acceptability, and that the conclusions expressed in Opinion No. 2 had not attained the degree of acceptability necessary to make it effective.

Five members of the Board, including Carman Blough and Leonard Spacek, dissented from Opinion No. 4. Eight of the majority assented with qualifications. These qualifications and dissents reflected a wide variety of viewpoints. An impression of internal chaos was created.

The prestige and authority of the Accounting Principles Board had been badly damaged in its first effort to advance the cause of comparability.

Field Day for the Press

The press had not been unaware of the controversy within the Board. The accounting profession and the Institute became targets for a barrage of public criticism unprecedented in the profession's history.

Business Week of January 26, 1963, published one of the first dramatic articles, entitled "A Matter of Principle Splits CPAs—Three of the Big Eight Accounting Firms Defy Their Trade Group on Fundamentals of Accountants' Role—A Wider Squabble Might Bring Intervention by SEC."

Reviewing the objectives of the Accounting Principles Board and the varying positions on the investment credit issue, the article stated that three prestigious firms had decided to ignore the ruling of the majority of the APB in its Opinion No. 2. This, said *Business Week,* amounted to "a calculated challenge to APB authority," which, in turn, was a reflection of a deep split within the accounting profession. One accountant was quoted as calling the position of the dissenting firms "prehistoric: this is the first time in my memory that a major firm has thumbed its nose at the recognized authority in the profession."

The article cited specific cases in which companies had in-

creased earnings by accounting changes which were permissible within the existing framework of generally accepted accounting principles.

The general impression conveyed by this article was that of a profession confused and angry—unable to come to agreement on its own proper role in conducting the independent audit function.

The New York Times, The Wall Street Journal, Forbes, Barron's, Fortune, and many other publications had their say. The "flexibility" of accounting principles was harshly criticized; the difficulty of comparing earnings of one company with those of another was mentioned frequently; the question whether auditors were truly independent of management was raised more than once.

The SEC's Position

In February 1963, Jack M. Whitney II, a member of the Securities and Exchange Commission, made a somewhat threatening speech before the Washington, D.C., Society of Investment Analysts. He said in part:

> A reliance upon "generally accepted accounting principles," as developed by the accounting profession, has left a great deal of room for variation in the accounting practices and principles observed by companies, whether or not they are subject to the requirements of the Commission. The unanswered question presented by this history, to which analysts might well help us find an answer, is whether the Commission's restraint has been and continues to be in the public interest and in the interest of investors. Do the disclosures of accounting principles followed, as contained in the prospectus, really make it possible for an analyst to make a side-by-side comparison of two competing companies' earnings statements? I doubt it. I do not suggest that unvarying application of uniform accounting principles is a desirable end in itself. I don't like straitjackets. However, we may not have gone as far in that direction as we should.

While it was made clear that Commissioner Whitney was expressing his personal views, and not those of the Commission, the quoted remarks were greeted with consternation by members of the accounting profession, in view of the SEC's failure to support the Accounting Principles Board's Opinion No. 2, which would have facilitated comparability of the earnings of competing companies.

However, William L. Cary, the chairman of the SEC, made a more reassuring speech before the Financial Executives Institute. Mr. Cary said:

> The SEC has been criticized for not supporting the Accounting Principles Board on the tax credit. . . . Regardless of the solution there, you may be assured the Commission's interest over the years has been to support the accounting profession . . . in narrowing areas of difference in financial reporting. This is still our view. . . .
>
> We all recognize the limitations of accounting, that absolute certainty is an absolute chimera—impossible to achieve. . . . Absolute comparability cannot be achieved because managements will still differ on basic practices—as, for example, how much money should be spent in any particular year on maintenance, advertising, or research and development.
>
> Nonetheless, despite any difficulties, you and we should direct our efforts toward accelerating the move toward uniformity. At the same time we should strive to make our disclosures more meaningful so that differences in accounting treatment are clearly brought out and better comparison of companies is possible.

However, still another slightly different approach was indicated by Byron D. Woodside, also a member of the SEC, in an address before the National Association of Accountants in June of 1964. He praised the accounting profession's "important role as a self-regulatory institution," and continued:

> We thought the dismay with which our reaction to the investment-credit episode seems to have been greeted, in some quarters, most unfortunate. We intended no rebuff to the profession or the Accounting Principles Board. On the contrary, we have encouraged and continue to encourage them in their work. We would caution, however, against the profession undertaking to do what you have always

pleaded that we not do . . . The task you set yourselves to force conformity on matters of accounting principles when there is not in fact acceptability of conformity, I think, is an impossible one. . . .

Those who wish to compel conformity—or rather seek to have us compel conformity—for only we in the final analysis have the tools to enforce the law or to set enforcement in motion—will no doubt be less than happy with this approach. What then are we left with, say they, except education and persuasion?

The short answer in our field of activity, I think, is that these have been the principal tools by which so much has been and continues to be accomplished. They have been the genius of the administration of the disclosure provisions of the '33 and '34 Acts. With your continued assistance I think they are likely, in major respects, to remain so.

This message seemed inconsistent with earlier exhortations by SEC spokesmen to speed up elimination of diversity in accounting practices which obstructed comparisons among different companies. Was the SEC softening its policy? To what extent would it back up the APB in efforts to eliminate alternative accounting practices?

Manual F. Cohen succeeded Mr. Cary as SEC chairman. One of Mr. Cohen's early speeches was before the American Accounting Association in 1964. He, too, referred to the differences of opinion over accounting for the investment credit, and, in particular:

. . . the fact that the SEC, consistent with its administrative policy on accounting matters, found substantial authoritative support for a method of accounting different from that announced by the Board as the majority opinion. The Commission was charged by some observers with an irresponsible act, but I can assure you that many hours of study and discussion preceded the decision to accept either of two solutions to this new problem in our experience. . . .

This episode has been discussed so vehemently that many persons seem to feel we have withdrawn our support of the profession's efforts to narrow the areas of differences in accounting principles. . . . This is not the case. It has been our practice for many years to cite publications of the Institute as authoritative support. . . . Exceptions have been rare indeed.

These statements from the Commission permitted the inference that the SEC would support Institute pronouncements except when there was strong opposition to them and substantial authoritative support for different conclusions.

In any event, the accounting profession was being made the whipping boy in the public press for everything that was wrong with corporate financial reporting. Corporate managements, held by the SEC to be primarily responsible for representations in financial statements, seemed immune from attack. Nor was the SEC itself the target of serious public criticism.

Leonard Spacek, who for many years had been waging a crusade for greater uniformity in financial reporting, was especially angered by the turn of events. In an address before the New York Society of Security Analysts in 1964, he stated the position bluntly:

> We have looked at the responsibilities of the financial analyst, the stock exchanges, and the SEC. None of them assumes responsibility for the adequacy and reliability of the financial information provided for the investors. What about management—the corporate officer?
>
> Everyone seems to agree that the corporate officer has primary responsibility for financial statements. Nevertheless, when a corporate officer is called upon to take responsibility for the accounting his corporation has made to stockholders, he invariably states that he relied on the corporation's public accountants to check the financial statements and give their opinion of the fairness of the statements. The corporate officer is not thereby relieved of responsibility for his misrepresentations, but it certainly helps to relieve him of any charge of negligence. . . . The investment community undoubtedly feels the monkey is squarely and firmly on the accountant's back.

The SEC Under Questioning

However, the SEC's role was questioned at a Congressional hearing. In 1963 and 1964, a subcommittee of the House of Representatives Committee on Interstate and Foreign Commerce conducted hearings on "investor protection." Specifically, the hearings were on proposed legislation resulting from

the SEC investigation of the securities markets, which had been conducted during the several preceding years.

One of the principal witnesses was Chairman Cary of the SEC. In the course of his testimony he was questioned by Congressman Harley O. Staggers of West Virginia, chairman of the subcommittee, on the subject of accounting principles. The following questions and answers ensued:

> MR. STAGGERS. Do you consider the financial statements now filed with the Commission are on a sufficiently sound and uniform basis to protect investors? . . . Who has the primary responsibility for the determination of appropriate accounting principles to be followed in the preparation of financial statements?
>
> MR. CARY. I think I can say quite truly that we have co-operated with the accounting profession very carefully on this subject over a period of years. I would take it as a joint responsibility. Mr. Barr has been working with them, I know, on an almost day-to-day basis over a period of years—particularly the American Institute of Certified Public Accountants. One of my colleagues says the ultimate responsibility is ours, but I think in many areas we have encouraged them to move ahead, and we have stood behind them. Sometimes we have differed, but in general we have been going along with them in many areas, and we have pushed them.
>
> MR. STAGGERS. I think it is one of the areas in which we must determine responsibility. Is it true that the Commission now accepts financial statements from various companies following alternative accounting practices with materially different results for similar transactions, and a certifying statement that all of these practices are in accordance with generally accepted accounting principles?
>
> MR. CARY. It is, sir. In other words, in some areas of accounting there are more than one, shall we say, accepted accounting principles applicable. In those cases we are in a position where we would accept more than one. . . .
>
> MR. STAGGERS. Do you consider that the Commission now has the responsibility of determining whether the accounting profession has taken appropriate action to determine adequate accounting principles?
>
> MR. CARY. I think we have that responsibility; yes, sir. And I trust we are exercising it. . . .
>
> MR. STAGGERS. Can you file with this committee a statement setting forth what you understand to be the areas of accounting where alternative practices could produce materially different results under generally accepted accounting principles?

Chairman Cary undertook to furnish a statement, and it was subsequently filed with the committee by Andrew Barr, chief accountant of the SEC, and reproduced as part of the record of the hearings. He listed the following areas of accounting where alternative practices could produce materially different results under generally accepted accounting principles: (1) valuation of inventories; (2) depreciation and depletion; (3) income-tax allocation; (4) pensions; (5) research and development costs; (6) goodwill; (7) time of realizing income; (8) all-inclusive versus current-operating-performance profit-and-loss or income statement. This list was accompanied by an explanation of the efforts of the accounting profession and the SEC to narrow the areas of difference in financial reporting.

Mr. Barr's statement contained other illustrations of areas in which alternative accounting practices existed: intercorporate investments; long-term leases; principles of consolidation; business combinations; income measurement in finance and small-loan companies and intangible costs in the oil and gas industries.

The very existence of this public record was a warning both to the SEC and the Institute to get on with the job.

The Council Acts

Institute members throughout the country were severely shaken by the internal dissension and by the widespread and sustained adverse publicity of which the accounting profession had become the object. President Witschey, the executive committee, and members of the Council were deeply disturbed. It seemed that the profession was in crisis.

In 1963 President Witschey submitted a statement to the Accounting Principles Board, and attended its meeting in April of that year, in an effort to clarify objectives and reach

agreement on procedures which would avoid repetition of the experience with the investment credit.

After discussion at subsequent meetings, the Board, by a divided vote, approved recommendations that members of the Institute be required to direct attention to any material variation between the accounting principles followed and the principles which the Board had approved, and that the auditing standards of reporting and the Code of Professional Ethics be amended to assure compliance with this new requirement. The vote on the motion was 11 in favor and eight against, with two members of the Board absent.

Among other possibilities, the Board considered whether the expression "generally accepted accounting principles" should be altered. Despite existing uncertainty as to the precise meaning of these words, however, the Board believed that the phrase was so widely used that it would be unwise to change it, and that such a change was not necessary to attain the Board's objectives.

The executive committee discussed this matter at great length. In view of the close vote within the Board, it was resolved that the recommendations approved by such a slim majority should not be forwarded to the Council at that time.

Later, however, the executive committee tentatively approved a proposal that Opinions on accounting principles issued by the Board should be regarded as generally accepted accounting principles, and that justification of departures from such Opinions should be incorporated in opinions of independent auditors.

Alvin Jennings had succeeded Weldon Powell as chairman of the APB. Mr. Jennings appeared before the executive committee to discuss this proposal from the Board's viewpoint.

The proposal was then exposed to the members of the principal committees involved, where a good deal of disagreement developed.

After consultation with legal counsel and further discussions, the executive committee finally issued modified recommendations to the Council in a special report dated March 14, 1964.

This report was entitled, "Status of Pronouncements of Accounting Principles Board."

The thrust of the executive committee's recommendations, from which three members of the committee dissented, was that "a pronouncement of the Accounting Principles Board, designated by it as embraced by this rule, shall be considered as constituting the only generally accepted accounting principle or principles in the subject area covered for purposes of expressing an opinion on financial statements, from the time it becomes effective, unless and until such pronouncement is rescinded by the Board or the Council."

The report contained detailed provisions, including suggested amendments to the Code of Professional Ethics and the bylaws, for implementation of this recommendation.

Provisions were included to protect an auditor from being required to express an opinion contrary to his own professional judgment, and to protect an auditor who expressed an opinion that statements conformed to generally accepted accounting principles within the meaning of the term as used in a statute, governmental regulation, or other legally controlling context, provided that the auditor's report in either case disclosed any departure from an APB Opinion, with appropriate explanation.

The executive committee's report included lengthy arguments both in favor of the proposal and against it.

This proposal was, of course, a radical change from the existing provision that the authority of APB Opinions rested upon their general acceptability; and from the policy declaration in the report of the special committee on research program, that reliance should be placed on persuasion rather than compulsion.

Clifford V. Heimbucher of San Francisco had succeeded Mr. Witschey as president of the Institute, and therefore as chairman of the executive committee and the Council. Mr. Heimbucher was senior partner of the local firm of Farquhar,

Heimbucher & Company, San Francisco. A man of unusual intellectual capacity, his demeanor was calm and unruffled. It was his duty to preside at the meeting of Council at Boca Raton, Florida, in early May of 1964, at which the executive committee's controversial recommendations were presented.

At this meeting the debate was the most animated, the most heated, and the most extended which had ever occurred at a meeting of the Institute's Council.

More than 40 members of Council, committee chairmen and members of the Accounting Principles Board participated in the argument, which lasted approximately eight hours.

The motion presented on behalf of the majority of the executive committee as a basis for discussion was as follows:

> A pronouncement of the Board constitutes the only generally accepted accounting principle for purposes of expressing an opinion on financial statements, unless and until rescinded by Council.

A spokesman for the majority of the executive committee stated that the proposal was designed to accomplish three things: (1) to give greater authority to Opinions of the APB; (2) to define more clearly the role of the profession in providing leadership in the development of accounting principles; (3) to strengthen and give meaning to the concept of generally accepted accounting principles, and to aid in eliminating undesirable and unnecessary differences in accounting practice.

He pointed out that a profession had to set its own standards, and that where private groups failed to set standards the government had stepped in to do it for them. He reminded the Council that the SEC had statutory authority to prescribe accounting principles, but so far had relied on the accounting profession. However, he warned that if public pressure became strong enough the SEC would have no recourse but to exercise its authority.

He quoted from press comments, magazine articles, and speeches, as well as testimony by the chairman of the SEC at the recent Congressional hearing, to illustrate growing

dissatisfaction with corporate financial reporting and with the accounting profession.

He said:

> Throughout this 25-year period, CPAs, business and financial executives, SEC spokesmen, educators and others have continued to say: (1) financial accounting and reporting need to be improved; (2) too many alternative methods and procedures are being used; (3) some limitation on the number of accepted alternatives is desirable; (4) some part of the solution lies in more carefully specifying "the principles of accounting." . . .
>
> "Generally accepted accounting principles" sound like something definite. Actually it means substantial authoritative support. This in turn indicates not only Institute bulletins and SEC releases, but also practices of the business community, textbooks and authoritative precedent. We cannot provide a satisfactory answer to the question, generally accepted by whom—the Institute; the corporations which are being audited; the textbook writers?

He said that the proposal before the Council would answer that question by saying that when an independent auditor used the term generally accepted accounting principles he would mean what his profession said it meant, " 'generally accepted' by the members of the national organization of CPAs. . . ."

He continued:

> It has been said that this proposal would substitute compulsion for persuasion, but in this case, compulsion to do what? Only to disclose deviation from generally accepted principles as the profession itself will have defined them after consultation with representatives of management, the SEC, the stock exchanges, analysts, bankers and anyone else who is interested. . . .

A spokesman for the dissenting minority of the executive committee suggested that the Council bear in mind the distinction between objectives, on which there would be general agreement, and the procedure for attaining those objectives, which was the essence of the proposal before the house. He warned against being swayed by general slogans or by fear that something "terrible will happen" if the pending proposal weren't adopted. He continued:

> What does the present proposal do? In essence, the proposal is that machinery be set up, the ultimate end of which would be to compel us, under penalty of disciplinary action under our Code of Ethics, to insert a qualification in our certificate when our own professional judgment is that such qualification is unnecessary or undesirable.

He pointed out that members already qualified their opinions when an Institute committee pronouncement had been violated and a client's method did not have substantial authority outside the Institute committee. The new proposal, he continued, would require qualification when the APB issued an Opinion which was highly debatable, and when a method not approved by the APB but which had other substantial authoritative support was selected by the client as more appropriate for it and this decision was concurred in by the auditor.

"It is when the APB-approved methods are thus on the ragged edge of not being generally accepted," he went on, "that you and I are to be compelled to state in our certificates that its methods are the only generally accepted accounting principles. Thus the change from the present practice, and the only one called for by the proposal."

He contended that approximately 95 per cent of the bulletins of the former committee on accounting procedure were followed in practice. Therefore, he said, the first condition for compulsory qualification under the pending proposal would be an APB Opinion which would be something of a "problem child from the outset. Opinion No. 2 on the investment credit is a good example." The second condition for compulsory qualification he said, would be when a client refused to follow the APB: "The client has the right to do this, for the financial statements are his, and he is the one that has to pay the damages if he uses an accounting method which a judge or jury decides has damaged someone."

The third condition for compulsory qualification would be, he said, when the auditor did not agree that the qualification should be there. Under existing conditions, if the auditor felt that the Institute bulletin embraced the only acceptable method he would qualify any departure from it.

The speaker declared that an auditor must state in his opinion what he honestly believed, both as a matter of professional integrity and in order to avoid the risk of liability. If an auditor honestly believed that the statements fairly presented the financial position and results of operations in accordance with generally accepted accounting principles, but if a client adopted a method different from one recommended by the APB, the new proposal would require the auditor to add to his opinion a statement that the client's method was not in accordance with generally accepted accounting principles. This, he said, would "violate the dictionary meaning of the words 'generally' and 'accepted.' "

He reminded the Council that corporations had the responsibility for their own financial statements and authority over them: the threat of qualifications in auditors' certificates would not compel companies to change reporting methods which they preferred. He continued:

> A rash of ill-founded qualifications, based upon unhappy APB pronouncements, could backfire on the profession in a manner frightening to contemplate. We must remember that auditors' opinions have not been considered essential in this country in important segments of the economy—banks, railroads and insurance companies, for example, as well as many small businesses. These companies have made out pretty well, by and large, without the auditors' certificates. . . . I suggest to you that ill-advised qualifications in auditors' certificates could weaken their value to the point where society could find them dispensable and look elsewhere for the attest function.

For three successive mornings, sincere and able men offered their views on the two positions which had been expressed. Past presidents of the Institute, senior partners of accounting firms, both large and small, and many members of the Accounting Principles Board itself took part in this discussion. The views expressed were widely divergent.

Proponents of the motion argued that the Accounting Principles Board could not accomplish its objectives if its pronouncements could be ignored; and that the executive

committee's proposal required only that auditors report deviations from effective pronouncements of the Board.

Some of the opponents expressed concern with what appeared to be an attempt by the Institute to appropriate the term "generally accepted accounting principles," which they considered to be in the public domain. Others attacked the complexity of the implementing procedures suggested to give effect to the basic proposal. Still others objected to the substitution of compulsion for persuasion.

Several proposed amendments to the motion were defeated. Finally the following substitute motion was offered:

> *Resolved,* That it is the sense of this Council that audit reports of members should disclose material departures from Opinions of the Accounting Principles Board, and that the president is hereby authorized to appoint a special committee to recommend to Council appropriate methods for implementing the substance of this resolution.

The motion was seconded. Discussion of the substitute motion continued. Finally the question was called for. The vote was 124 members of Council in favor of the substitute resolution, and 51 against it.

The chairman announced that in accordance with the resolution he intended to appoint a committee of no more than five distinguished leaders of the profession, none of whom was on the executive committee and none of whom was or had been a member of the Accounting Principles Board: he would ask them to review the entire matter *de novo,* and the first item of source material that he would give them would be the complete transcript of the discussion at this meeting.

The Special Committee

On May 21, 1964, shortly after the great debate at the Council meeting, President Heimbucher appointed a special committee of which William W. Werntz was named chair-

man. To the deep regret of all concerned, in the midst of the committee's deliberations Mr. Werntz suffered a heart attack and died. J. S. Seidman was then named chairman of the committee, which also included the following: Carman G. Blough; Albert J. Bows, a recent chairman of the committee on auditing procedure; Paul Grady, then the Institute's director of accounting research; John R. Ring, a recent chairman of the committee on professional ethics; Maurice H. Stans, a past president of the Institute; and Glenn A. Welsch, a recent president of the American Accounting Association.

At the annual meeting of the Institute in the fall of 1964, the special committee submitted its recommendations, which, together with subsequent developments, will be described in the next chapter.

CHAPTER 6

Increasing Authority of the APB

THE Council resolution adopted in May 1964, calling for disclosure of departures from APB Opinions, established a new and vitally important policy. Just how that policy was to be put into effect was the question referred to the distinguished special committee appointed by President Heimbucher.

That committee labored hard and long throughout the summer. At the Council meeting immediately preceding the Institute's annual meeting in the fall of 1964, the committee presented its report.

The report stated that generally accepted accounting principles were those principles which had substantial authoritative support, and that Opinions of the Accounting Principles Board constituted substantial authoritative support; however, substantial authoritative support could exist also for accounting

principles that differed from Opinions of the Accounting Principles Board.

The report continued, "If an accounting principle that differs materially in its effect from one accepted in an Opinion of the Accounting Principles Board is applied in financial statements, the reporting member must decide whether the principle has substantial authoritative support and is applicable in the circumstances."

If the answer to this question were negative, the report said, the member would qualify his opinion, disclaim an opinion, or give an adverse opinion as appropriate; if the alternative principle did have substantial support, he would give an unqualified opinion, but would disclose the fact of departure from the APB Opinion and, where practicable, disclose its effects on the financial statements. The member would make such disclosure in a separate paragraph in his report or see that it was made in a footnote to the financial statements.

Illustrative language for this purpose was provided.

It was further stated that Council's action calling for disclosure of departures from APB Opinions was not intended to have the force and effect of a rule of ethics, but rather that of a standard of reporting practice, deviations from which should have the attention of the practice review committee.

It was suggested, however, that further study should be given the question whether the Code of Professional Ethics should be amended to cover infraction of the committee's recommendations.

At the Council meeting there was surprisingly little opposition to the special committee's proposals. Many of the 51 members who had voted against the basic resolution at the previous spring meeting apparently felt that they could live with the implementing provisions submitted by the committee.

After some discussion the report was approved by a vote of 163 in favor and none against, though a few may have refrained from voting.

The Institute's annual meeting convened two days later. In his address to the members as retiring president, Clifford Heim-

bucher referred to the Council's action and added the following comment:

> . . . None of us would claim that accounting practice today is final, complete and perfect. None would claim that there is no room for further improvement. Many accounting problems remain to be solved. No single individual or organization has a corner on truth. These problems will be solved by co-operative, democratic effort carried on in an atmosphere of mutual respect and trust. Our profession should and will play a leading part, but it cannot do the job alone. And it cannot be done by fiat. The joint effort of many of the finest minds is necessary. . . .
>
> This action [by the Council] constitutes another and an historic step forward in the long, continuous process of improving financial reporting which has already brought us to the point where the American investor is the best informed investor in the world.

The special committee's recommendations as approved by Council, were published in a special bulletin issued by Thomas D. Flynn, the new president of the Institute, under date of October 1964, and sent to all members.

In May 1965 the special committee submitted a final report to the Council, including eight major recommendations related to the composition, procedures, and activities of the Accounting Principles Board.

Among the most important was Recommendation No. 2, calling on the Board to recognize the objective that variations in treatment of accounting items generally should be confined to those justified by substantial differences in factual circumstances.

This and most of the other recommendations were accepted by the executive committee and the Accounting Principles Board itself and were approved by the Council.

Action was deferred on a proposal that the new disclosure requirement be incorporated in the Code of Ethics and on another recommendation related to financing the Board's activities.

Clifford V. Heimbucher succeeded Alvin R. Jennings as chairman of the APB. Encouraged by the Council's expression

of confidence, and the strengthening of the Board's authority, its members turned their attention to the numerous and complex problems on its agenda.

Observations From the SEC

Immediately following the events described above, Byron D. Woodside, a member of the Securities and Exchange Commission, delivered an address before the fourth annual accounting forum of Hayden, Stone Incorporated, November 18, 1965. Mr. Woodside had lived through almost the entire period in which the SEC's policies on accounting and auditing had evolved. His observations were significant.

Mr. Woodside traced the history of the SEC's approach to accounting requirements, first stressing the Commission's powers to prescribe accounting rules for registrants. Then he eloquently expressed the importance of sound accounting: "History, common sense and experience tell us that at the heart of our whole system of securities markets . . . are faith and trust in the honesty of corporate financial records, and the honest, objective and timely distillation of those records in published financial statements. . . . One who weakens that trust without good cause does no one a service. One who trusts a system which really is not serving well its purposes may on occasion be deceived."

Referring to early abuses which needed correction, he continued: "Most of the matters they mentioned in those days as representing serious flaws in need of correction, and many of the problems which then seemed to call for rules by the Commission, have long since ceased to be problems or are now rarely so. . . . Solutions . . . have been accomplished by the operation of a system which I think has been quite effective despite the absence of the rule-making that then seemed perhaps inevitable." This "system," he explained, was a deliberate policy choice—a policy of co-operation with issuers and the

profession in a case-by-case approach: "The accountants in particular have asked for the opportunity to grow and develop free of rules."

Mr. Woodside then came to the question of comparability:

> Consistency of reporting for different periods by the same issuer has been emphasized. We have recognized, however, that, as between different issuers which may or may not be otherwise comparable, alternative accounting procedures with respect to a particular accounting presentation might be employed if there was—to quote Release No. 4 again—substantial authoritative support for the practice followed. I think it is fair to say that we have not sought to insure as an end in itself that the financial statements of Company A were comparable in all material respects with those of Company B. It may be that Accounting Release No. 4 is too simple and unsophisticated as a statement of administrative policy for a more complex age. It may also be that we should have made greater use of our accounting series releases for the purpose of announcing firm policies on more accounting matters.

Most significantly, the Commissioner said it would become increasingly difficult for the SEC to continue to rely on substantial authoritative support and the disclosure principle if members of the academic and practicing branches of the accounting profession continued to join other critics in emphasizing the noncomparability of corporate financial statements.

Mr. Woodside suggested strongly that issuers of financial statements had learned to exploit the confusion about accounting principles for their own purposes: "A not unusual situation is one where the management goes off on an accounting frolic of its own in its reports to the press or its stockholders, when it knows, or could easily find out, that it was following a practice not consistent with the best practice in its own field." Later this management would seek for and perhaps discover "authoritative support" for what it had done, he said.

On the efforts of the accounting profession, Mr. Woodside offered friendly comment: "My review of accounting literature leads me to conclude that that literature reflects consid-

erable voluble confusion. It is my impression that no proposition can be proposed for discussion for which there cannot be produced a multiplicity of plausible contentions reflecting every shade of opinion."

In short, this spokesman for the SEC seemed to be saying (1) that financial reporting in which the public had confidence was essential; (2) that most of the abuses of the early days had been corrected; (3) that this had been accomplished by the case-by-case approach, based on the concepts of substantial authoritative support and full disclosure; (4) that comparability had not been the Commission's primary objective; (5) that the approach of the past might be too simple for a more complex age; (6) that the SEC felt the pressure for greater comparability; (7) that management sometimes exploited the authoritative-support concept; (8) that the confusion and disagreement within the accounting profession was not encouraging; and (9) that the SEC might have to engage in more extensive rule-making unless the accounting profession got there first.

A Proposal for an Accounting Court

About a month after Mr. Woodside's speech the firm of Arthur Andersen & Co. published a pamphlet entitled, "Establishing Accounting Principles—A Crisis in Decision-Making." This pamphlet had been in preparation for a long time.

An extensive preamble reviewed the sources of accepted accounting principles, including the Institute, the SEC, and the American Accounting Association, and concluded: "The fact is that accounting principles have not been established on a truly authoritative basis by anyone." Accordingly the pamphlet proposed, for discussion purposes but without recommendation, that consideration be given to creation of a United States Court of Accounting Appeals.

Mr. Spacek, the senior partner of Arthur Andersen & Co.,

had proposed an accounting court in speeches of previous years, but had not presented a specific plan. The new pamphlet contained a draft of a bill to establish such a tribunal.

The proposal envisaged a court of five members appointed by the President of the United States, having jurisdiction over accounting rules of the five federal agencies primarily concerned with accounting principles—the Securities and Exchange Commission, the Federal Power Commission, the Interstate Commerce Commission, the Civil Aeronautics Board, and the Federal Communications Commission.

On petition, the court could review an accounting rule of an agency and affirm, modify or reverse the rule or remand it to the agency for further proceedings. All parties to the proceeding would be entitled to file briefs, and to be heard in oral argument, subject to rules of the court. Appeals from the court's decisions could be made to higher judicial authority.

The court's jurisdiction would not involve rate-making activities, but would be confined to accounting rules.

This proposal was discussed in accounting circles, formally and informally, but no official action was taken on it.

In a speech before the Temple University Accounting Forum in October 1965, shortly before this pamphlet was released, Mr. Spacek had advocated the establishment of an accounting court in order to eliminate uncertainties as to the meaning of generally accepted accounting principles. Another speaker at the same meeting was Thomas D. Flynn, one of the senior partners of Arthur Young & Company, who had just completed his term as president of the Institute. Mr. Flynn, during his presidency, had worked hard in support of the Accounting Principles Board. He had made numerous speeches to financial executives, bankers and other groups in an effort to secure co-operation in the Institute's efforts to improve financial reporting.

When he and Mr. Spacek had finished speaking at Temple University, the floor was thrown open for questions. A participant asked Mr. Flynn what the economic effect on the practice of certified public accountants would be if the accounting

court proposed by Mr. Spacek were established. Mr. Flynn answered the question by asking another—whether the proliferation of laws and court decisions had tended to reduce the income of lawyers.

The implications of this response were significant. If accounting principles were to be established by government regulation or judicial decision, there would still be room for honest differences of opinion. But much more important, Mr. Flynn pointed out that there would be a proliferation of intricate rules and regulations designed to deal with a wide variety of complex economic and business situations. There would be substantial gaps between the literal interpretation of these rules and regulations and a realistic view of the economic facts which should be reported to the users of financial statements—and just as attempts to simplify the Internal Revenue Code have led to increasingly complex provisions, so would the rulings and decisions of the Accounting Court lead to an increasingly complicated mass of accounting precedents in which only the expert could tread. Mr. Flynn went on to say that there would be plenty of work for accountants in advocating before an accounting court the promulgation of principles which they believed superior to those proposed by others. Once a court had established principles, he believed that there would be even more work for independent auditors to interpret the findings, and appraise the judgmental decisions which must be made in their application in the circumstances of particular cases.

But it seemed clear to many observers that while the accounting profession would not suffer, the transfer of authority to determine accounting principles from the private sector to a government tribunal could have grave implications for a free-enterprise economy.

At the same time it was not yet clear that the profession's leadership in the development of accounting principles was secure. The concern of the SEC, and the differences of opinion within the profession, raised doubts about the future course of events.

The Council's resolution that departures from ABP Opinions should be disclosed was generally regarded as a forward step. But it was widely noted that up to that time the Board had issued only six Opinions, two of which dealt fruitlessly with the investment credit, and one of which incorporated as an Opinion of the Board those portions of the earlier Accounting Research Bulletins which were still regarded as authoritative. In the six years of the Board's existence, the progress in resolving major problems was not impressive in the view of many observers.

Furthermore, there was as yet no certainty that the profession was united on a common objective.

Uniting on a Common Objective

Emotional tensions had been aroused which interfered with clear communication. Those who were convinced that existing obstacles to comparability of earnings must be removed were accused by others of advocating "uniformity" in accounting—putting accounting in a straitjacket which would impede progress.

Those who were opposed to "uniformity," on the other hand, were accused of advocating "flexibility" in accounting. Their adversaries interpreted this as a desire to give management the widest possible choice in selection among alternative accounting principles, thus unnecessarily impairing comparability of the results of one company with those of another.

Actually, neither group took positions as extreme as their opponents inferred. Leonard Spacek, for example, was an outspoken advocate of "uniformity." Yet it became clear that when he used that word he was referring to principles as distinguished from methods.

He agreed with an earlier statement by Alvin Jennings that criteria should be established to determine the circumstances under which one method resulted in a fairer presentation of

net income than another method: there could be various methods from which to select under such criteria, in order best to reflect the circumstances, but there should not be alternative principles.

In a 1965 speech Mr. Spacek said:

> I would like to emphasize . . . that I am not talking about an accounting straitjacket, or a detailed bookkeeping rule book which would attempt to make dissimilar conditions or circumstances appear to be similar. What I am talking about are accounting principles, criteria and guidelines for use by industry and by accountants that would represent a common standard and would be applied on the basis of judgment to the wide variety of circumstances found in business . . . . the variations in reported earnings and other financial information would result more from variations in conditions and facts and not so much from variations in accounting methods selected from the wide assortment available today.

When Robert M. Trueblood was elected president of the Institute in the fall of 1965, the heat generated by the debates of the preceding years had not yet been fully dissipated. To be sure, the report of the special committee on Opinions of the Accounting Principles Board had been found acceptable for the most part, both to the executive committee and to the Accounting Principles Board itself, and on their recommendation the Council had approved it—including the significant provision that the objective was to confine variations in treatment of accounting items generally to those justified by substantial differences in factual circumstances. However, there was still doubt whether this objective was acceptable to all accounting firms, or indeed whether it would be interpreted in the same way by all members.

Mr. Trueblood was chairman of the policy committee of Touche, Ross, Bailey & Smart. He was a man of action, with unusual intellectual attainments, which had been amply demonstrated in a long period of service to the profession in many capacities.

He decided to attempt a reconciliation of the opposing views. Accordingly, he took informal soundings among partners of

various accounting firms and other influential members, representing both the so-called "uniformity" and the so-called "flexibility" schools of thought.

To his great satisfaction, President Trueblood found that there were broad areas of agreement. Essentially it was agreed that the objective was to reduce the number of alternative accounting practices not justified by actual differences in circumstances. It was also agreed that this could not be done quickly over a broad range of problem areas, but that while alternatives were being minimized progress could be made through improved disclosure requirements. However, disclosure requirements should not be regarded as a substitute for the reduction of alternatives wherever this was logical and feasible.

No one, it was found, advocated a uniform chart of accounts for industry as a whole, or for specific industry groups. It was agreed that the function of the Accounting Principles Board was not to prescribe the details of accounting, but to develop sensible criteria which in similar situations would lead to similar results.

With this encouragement, Mr. Trueblood, in his capacity as president, made a statement to the Council at its meeting in the spring of 1966, which did much to clear the air. He said, in part:

> For the past few years I have been concerned, as you have surely been, about the matter of accounting principles; about the questions and criticisms appearing in the press; about the doubts which such comments must arouse among people outside our profession; and about the possible divisive influences which could develop within the profession over the philosophical issues which seem to be of concern.

He cited comments in the press, including a quote from the vice chairman of the First National City Bank, ". . . the accounting profession cannot say precisely—or perhaps even approximately—what . . . generally accepted accounting principles are."

Mr. Trueblood spoke of the differences of opinion over the

concepts of comparability and uniformity. He reviewed the work of the Accounting Principles Board and expressed confidence that it could do the job.

"Our overall objective," he said, "clearly articulated in the Seidman report, is to reduce the number of alternative practices not justified by actual differences in circumstances." While the Board was pursuing this objective, he said that progress could also be made through disclosure requirements, but compliance with Board Opinions as they were issued was of crucial importance.

In conclusion, he expressed the view that disagreement was not nearly so wide as publicity had indicated. He believed it to be the unanimous view of the membership that the objective of the APB was not to get out a series of rule-books, but rather to recommend accounting practices "which will make like things look alike, and unlike things look different."

In conclusion, Mr. Trueblood said, "I am of good cheer. I think that the criticism our profession has undergone has not been without its blessings . . . we have made substantial progress in improving the tools we use in serving society. And, I am convinced, we are on the threshold of still greater accomplishments."

These remarks were received by the Council with great enthusiasm. On motion duly seconded, it was resolved that the president's statement should be printed and sent to all members of the Institute, which was done.

At long last there was hope that confusion over the goals of the Institute in the development of accounting principles had been resolved and that the profession had regained its bearings.

Increased Pressure From the SEC

It was high time that the profession agreed on clear objectives.

SEC spokesmen had resumed their appeals for greater speed

in the quest for comparability through elimination of less desirable accounting practices.

In particular, Manuel Cohen, the new chairman, began to take a tougher line than his predecessor. In 1965, he had said in an address before the Investment Bankers Association:

> While some action has been taken by the accounting profession, the overall picture is not encouraging. . . . We are now considering some limited action of our own in this area—action which is not designed to undermine the efforts of the leaders of the profession, but rather to emphasize to the entire profession the urgency of immediate and effective support of those who are seeking sound procedures to obviate unjustified differences in the treatment and presentation of similar problems.

Mr. Cohen was undoubtedly referring to a pending decision of the SEC to issue a statement on the treatment of deferred taxes on installment sales. This question was before the Accounting Principles Board and, in fact, a tentative decision had been approved, but in deference to spokesmen for the retail industry, issuance of an Opinion on the matter had been deferred in order to give them an opportunity to submit their views.

Arthur Andersen & Co., however, had petitioned the SEC to rule on the matter. The chairman of the APB had requested the Securities and Exchange Commission to defer action, but the Commission proceeded to issue Accounting Release No. 102, which settled the question, much to the dissatisfaction of the industry most concerned.

In a later address before the Financial Analysts Federation in 1966, Mr. Cohen referred to this incident. In preliminary remarks he said:

> The importance of comparability of financial statements is apparent. Not only are statements used to compare the same company at different time periods; they are used to compare similar companies with each other and these comparisons can be of great significance. . . . One of the principal obstacles to comparability of financial statements has been the application of alternative accounting principles

> to similar sets of facts. . . . And we have looked primarily to the accounting profession for formulation of those principles. . . .
>
> The accounting profession has not resisted the freedom, and concomitant responsibility, given to it by the Commission to develop accounting principles. There are many who believe, however, that the accountants have not fulfilled that responsibility. Without minimizing the difficulties of the task, and with no intention to criticize, it is fair to say that the accounting profession has, in the past, been unable to achieve uniformity in many significant areas of financial reporting —that is, accountants have been unable to reduce significantly, if not eliminate, the variety of accounting principles deemed permissible in the reporting of similar financial conditions and results.
>
> What is being done about moving more quickly toward the goal of uniformity? Stronger leadership by the Commission is one avenue being followed. An example of this is Accounting Release No. 102 issued a few months ago, dealing with the proper method of reporting deferred income taxes arising from installment sales. . . .
>
> The American Institute of Certified Public Accountants had not ignored the problem, but had up to then been unable to resolve it. . . . A formal expression of opinion by the Commission seemed called for, and we obliged. . . .
>
> Although Accounting Series Release No. 102 was used to resolve one problem of uniformity, I do not believe it will be necessary for us to use that device with great frequency—although the option is always open to us. The extent to which action on our part is required will depend in large measure on the vigor and determination of the Accounting Principles Board of the American Institute of Certified Public Accountants, which has the principal responsibility of defining accounting principles to be used in financial reporting. I am greatly encouraged by the current activity and progress being made by the Board.

The warnings seemed to be louder and clearer, and they were backed up by action. Later the Commission issued two releases taking positions on accounting questions which were under the consideration of the Accounting Principles Board, but on which it had not yet acted. One dealt with reporting by separate lines of business, widely thought to be directed at so-called conglomerates, and the other dealt with the treatment of convertible securities as residual securities in determining earnings per share.

Industry Resistance

While the Accounting Principles Board eagerly sought the co-operation of industry in eliminating unnecessary obstacles to comparability of earnings, and while industry groups with equal eagerness sought an opportunity to be heard on all Board proposals, the result was more often opposition to proposed Opinions than constructive suggestions for solution of pending problems.

For example, in 1967 the APB exposed for comment a draft of an Opinion on "Accounting for Income Taxes," a major problem area which had been prominently mentioned by Andrew Barr, chief accountant of the SEC, in response to a Congressional committee's inquiry, as one in which diverse practices impeded comparability of earnings. The proposed Opinion dealt with two major issues: (1) allocation of income tax on differences between taxable income and income reported in financial statements; and (2) the investment credit, which under Opinion No. 4 remained a sore thumb, with alternative methods permitted in identical circumstances.

In preparation of the draft Opinion a subcommittee of the Board had met with 24 separate industry groups and government agencies, all of whose views were well known to the Board and had been given consideration.

The Financial Executives Institute and other industry groups organized letter-writing campaigns in opposition to the Opinion. Almost a thousand negative letters were received by the Institute, and copies of many of them went to the SEC. Most of the letters objected to the Board's proposal for accounting for the investment credit, but significant numbers of them also objected to the proposal for allocation of income taxes.

The firm of Price Waterhouse & Co. published a pamphlet, which was widely quoted in the press, also arguing against the Board's proposal for comprehensive income-tax allocation.

Lacking assurance that the SEC would support a firm position on the investment credit, and unwilling to risk the

necessity of reversing itself a second time, the Board dropped the section dealing with this troublesome matter. Despite the strong opposition to comprehensive tax allocation, however, the Board issued Opinion No. 11, which decidedly narrowed the areas of difference in accounting for income taxes.

On another occasion the fire-and-casualty insurance industry mounted an all-out pressure campaign to prevent a technical committee of the Institute from issuing an audit guide, cleared by the APB, recommending changes in accounting practices followed by that industry in order to provide better information to investors—notably a matching of policy acquisition costs with related premium income. The guide was published nonetheless, but not until after years of inconclusive argument.

Later, the American Bankers Association opposed a proposed Opinion of the Accounting Principles Board which would remedy widely criticized flaws in the financial reporting of banks, particularly by requiring a net income figure after charges for bad-debt provisions and losses on sales of securities. The president of the American Bankers Association wrote a letter to all member banks, advising them to accept qualifications in auditors' reports rather than conform to the proposed APB recommendation. After further conferences with bankers and the bank regulatory agencies, however, the Board issued Opinion No. 13 in 1968, applying to banks the same income-reporting principles as those applicable to industrial companies, as set forth in its Opinion No. 9. Acceptance of this pronouncement by bankers and regulators was not obtained until more than a year later, after implementation rules were worked out through joint efforts.

Various groups, including investment bankers, also resisted proposals by the Board relating to potential dilution of earnings per share through convertible securities and warrants. This problem was ultimately dealt with in Opinion No. 14 in 1969.

Few APB pronouncements escaped opposition from some corporations or industry groups which would be required to change their customary accounting methods. But the APB

was facing the fact that it couldn't please everyone. Its mission had been clarified; its Opinions had been given greater authority by the Council's resolution calling for disclosure of departures from them; and the internal dissension triggered by the investment-credit incident was subsiding. The profession was again united behind it, and the Board began to recognize that it had acquired real authority—and with it the responsibility to move toward the announced goals in spite of inevitable opposition.

The Press Keeps Score

Fully awakened to the significance of accounting principles to the investment community, the financial and business press kept close watch over the Accounting Principles Board during the crucial years following its unsuccessful effort to deal definitively with the investment credit.

Gradually, however, the highly critical tone of earlier comment was modified. The successive Opinions of the Board were reported with respect. Reference to "the influential Accounting Principles Board," and similar expressions, appeared with increasing frequency.

However, the public interest in the accounting profession's problems was highlighted by a few widely publicized lawsuits against accounting firms, involving well-known companies, in the mid-1960's.[1]

The result was a series of articles mixing references to the pending litigation with comment on the tribulations of the Accounting Principles Board.

Rehashes of what came to be known in some quarters as

[1] Since at the time of this writing these suits have not been decided, any effort to describe the issues, or the legal effect of possible decisions, would be inappropriate here. This must await the deliberate analysis of legal counsel. For these reasons no chapter on accountants' legal liability appears in this volume.

the "investment credit fiasco" appeared in many of these articles. Almost every prestigious financial or business magazine, and almost every columnist who dealt with financial matters, found it necessary to publish a critical re-examination of the accounting profession in general, and its "generally accepted accounting principles" in particular.

An editorial in *Forbes* magazine stated that "generally accepted accounting principles mean damn little."

The same magazine later published a lengthy article entitled "What *Are* Earnings? The Growing Credibility Gap." "For decades the accounting profession basked in the highest kind of public confidence," the article began. "Now . . . a barrage of public criticism has landed on the profession for its highly flexible 'generally accepted accounting principles'. . . . What people are now beginning to understand is that these earnings figures as determined under the so-called generally accepted accounting principles are far from precise, nor are they exactly comparable with those of other companies. What's more, they never have been."

However, the APB was given credit for several strong Opinions recently issued.

Under the title "CPA Under Fire," *The Wall Street Journal* published an article which said in part: "The independent firms that audit the books for American business are now under unprecedented attack, and their image of sober rectitude has already suffered damage that may take years to repair. . . . The events of recent months . . . suggest that the government, the courts, and the mounting pressure of adverse public opinion may force them to move faster and further than anyone expected—and in some cases, take the decisions out of their hands."

The writer said that the responses of the auditors to criticism "seem like whispers in a whirlwind." Latitude in accounting principles was described as "wide as a whale's mouth. . . . It's often impossible to meaningfully compare one company's results with another's."

This article, however, did refer to increased activity on the

part of the Accounting Principles Board, which was considering Opinions which "will have considerable force." Reference was also made to the new requirement that auditors should disclose departures from APB Opinions. However, the article continued, "though the profession is trying harder to clean its own house, the pace has been too slow for many critics, notably the SEC."

Under the title, "CPA Audits and Gobbledygook Guides," *The Wall Street Journal* published another feature article beginning, "When a Certified Public Accountant audits a corporation's financial records, does his first allegiance lie with the stockholders or with management?

"Most CPAs answer this decades-old question unhesitatingly. 'With both,' they snap. Then they add that their basic duty is to certify that the corporation's annual reports conform to generally accepted accounting principles."

The article went on to question whether "the role the CPA has carved out for himself conflicts with the basic reason his job as independent certified public accountant was created in the first place." The writer suggested that critics of current auditing practices maintained that the CPA should take on the job of "policeman."

Favorable reference was made to a recommendation of the Institute's executive committee that auditors be nominated by audit committees of boards of directors, composed only of outside directors who were not a part of management. Such audit committees could suggest changes of auditors, could check whether undue restrictions were being placed on auditors, or could advise the boards of directors whether questions about financial statements should be reported to stockholders, stock exchanges, or the SEC.

Critical articles also appeared in law-school publications. An issue of *Law and Contemporary Problems,* published by the Law School of Duke University, was entirely devoted to articles on the accounting profession and its role in the development of accounting principles. Several of the articles were highly critical. Later, the *Columbia Law Review* published a lengthy

note, written by law students, in which were extensive quotes from articles in *The Wall Street Journal, Forbes,* and other sources, putting the profession in a highly unfavorable light. The conclusion of the authors was that the public was inadequately protected, and that heavier legal liabilities should be imposed on the accounting profession. In still another article by law students in the *Washington Law Review,* it was suggested that if the Accounting Principles Board could set appropriate standards, they would serve as a protection against liability to auditors who observed them. The implicit conclusion, however, was that if the Board did not make progress rapidly enough, the courts themselves would have to decide what was appropriate accounting in the circumstances of particular cases.

As late as January 8, 1969, *The Wall Street Journal* published a lengthy article entitled "Frustrated CPAs—Accounting Body Fails in Attempts to Change Some Firms' Reporting." The article said in part:

> . . . Company resistance has led the accounting profession to back down on several proposals to change the ways many companies tally and report profits. . . . Some accountants fear the backdowns add up to a serious setback for a seven-year-old drive by the American Institute of Certified Public Accountants to standardize corporate reporting. . . . In the last year or so, the AICPA's rulings have provoked increasingly vehement protests from company officers. And the accounting body has bowed to the pressure—too quickly, some critics charge—in three cases.

The article listed the three cases: the proposal on the investment credit which was withdrawn from APB Opinion No. 11, the proposal for changes in the financial reports of banks which was still under discussion, and the suspension and impending reversal of the requirement in APB Opinion No. 10 of assigning value to the conversion feature of convertible securities (the latter two being the subject of Opinions issued a few months later).

After describing the impact that these Opinions would have had on reported profits, the article continued:

> The AICPA's failure to make this and the other rulings stick, points up a basic weakness in its position: It cannot enforce its rulings against a company willing to issue a report containing an auditor's statement of exception to some of the figures. . . . Some financial men . . . are keenly disappointed that the AICPA backed down on these issues. . . . Analysts think the AICPA could enforce greater uniformity if it were willing to fight. . . .

While these comments were not well founded, they pointed up the fact that the Accounting Principles Board was making a sincere effort to discharge its responsibility; and that corporate management was partly to blame for the delays in moving forward.

Most significant was the implied acceptance of the Board's power.

The APB's Achievements

The press and the public did not yet fully realize that the Accounting Principles Board was making substantial progress in the improvement of financial reporting, and in facilitating comparability of earnings.

Off to a slow start by waiting for research studies, and further delayed by controversy over the investment credit and basic policies, the Board's production was truly impressive in the five-year period, 1964 to 1969.

Even before the action of Council in 1964, the Board produced two constructive Opinions. Under Alvin Jennings' chairmanship, the Board issued in 1964 Opinion No. 3 on "The Statement of Source and Application of Funds," based on Perry Mason's research study, to which reference was made in Chapter 5. This Opinion received wide support in the financial community. The president of the New York Stock Exchange sent copies to the presidents of listed companies and to all members of the Exchange, recommending that the Opinion be followed in reports to stockholders. On the basis of

this Opinion, also, financial analysts began to discourage figures indicating "cash flow per share," as misleading to investors.

Also in 1964, the Board issued Opinion No. 5, "Reporting of Leases in Financial Statements of Lessee," extending disclosure requirements, and providing criteria for identification of lease agreements which were in effect installment purchases which should be capitalized. This Opinion did not satisfy all critics of accounting for leases, but it was a step forward.

Under the chairmanship of Clifford Heimbucher, the Accounting Principles Board underwent a partial reorganization in 1965, following Council approval of the Seidman committee report.

A new staff position was created—administrative director of the Board—which was assumed by Richard C. Lytle, formerly the Institute's director of technical services. He engaged several assistants. This step relieved Reed Storey, who had succeeded Paul Grady as director of accounting research, of responsibility for assistance in execution of the Board's functions, and enabled him to concentrate on the production of research studies.

The Board itself was divided into subcommittees, each one assigned a designated subject on which to prepare recommendations for consideration of the full Board.

A planning subcommittee was created to review projects, schedule priorities, and fix target dates.

Arrangements were made for periodic meetings with the members of the SEC and its staff, at which progress was reported and pending problems were discussed.

A program was developed to encourage more effective participation by industry and government agencies in the efforts to improve financial reporting. This involved meetings with many such groups and wider circulation of both research studies and "exposure drafts" of APB Opinions.

All this added to the burdens of Board members. The number of Board meetings was increased—there were seven in 1966, each of them lasting three days. There were also, for

example, 26 subcommittee meetings between September 1965 and May 1966.

But the work was not in vain. Results began to be visible.

The main job of the reorganized APB in 1965 was to review the Accounting Research Bulletins produced by the former committee on accounting procedure, and decide to what extent disclosure of departures from them should be made under the Council's resolution. The resulting Opinion No. 6, "Status of Accounting Research Bulletins," was issued in October 1965.

Opinion No. 7, "Accounting for Leases in Financial Statements of Lessors," was issued in May 1966.

A major breakthrough occurred in 1966, with the publication of Opinion No. 8, "Accounting for the Cost of Pension Plans," and No. 9 "Reporting the Results of Operations." The pension Opinion greatly narrowed the range of methods of accounting for pension costs, and eliminated "pay-as-you-go" accounting by requiring accrual of provisions for pensions on a systematic basis. This did away with many diverse practices which had impeded comparability of earnings, and was hailed by the chairman of the SEC and the president of the New York Stock Exchange as a major contribution to improved reporting. Favorable press comment followed.

The Opinion on results of operations was also favorably received by the Commission, the Exchange, and, with a few exceptions, by the press. This Opinion finally settled the difficult problem of treating extraordinary items and prior-period adjustments without distorting income from recurring operations. Also for the first time Opinion No. 9 took the position that the potential dilution of earnings per share by conversion of convertible securities should be indicated in financial statements.

Opinion No. 10 was an "omnibus" Opinion, covering a number of specific items not deemed of sufficient importance to justify separate Opinions.

In December 1967, in the face of strong opposition the Board issued Opinion No. 11, "Accounting for Income Taxes" (see pages 133 and 134).

Opinion No. 12, issued in the same month, was a second "omnibus" Opinion, dealing with six specific questions.

Thus, through 1967 the APB had published 12 Opinions, in addition to a special statement, "Disclosure of Supplemental Financial Information by Diversified Companies," containing preliminary observations on product-line reporting by conglomerates.

In the same period the research division had produced nine research studies, of which a total of 362,000 copies had been distributed. Eight additional research projects were in process.

Among the published research studies was the massive "Inventory of Generally Accepted Accounting Principles for Business Enterprises," written by Paul Grady while he was director of accounting research. This study classified and explained the accounting principles believed to be generally accepted—to have substantial authoritative support—at the time of publication. The study served not only as a convenient reference to analysts of financial statements, but as a basis for examination of areas in which diversity of practice existed and which therefore needed the attention of the Accounting Principles Board.

Opinions No. 13 and No. 14, issued in 1969, dealt respectively with bank accounting, and accounting for convertible debt and debt issued with stock purchase warrants, as mentioned previously.

The Board was well on its way to successful discharge of its mission, and its prestige and authority were growing year by year.

The Seaview Symposium

The increased authority of the Accounting Principles Board was recognized informally at a Symposium on Corporate Financial Reporting held in 1968 at the Seaview Country Club,

Atlantic City, New Jersey. The participants were selected representatives of the Financial Executives Institute, the Robert Morris Associates, the Federation of Financial Analysts and the American Institute of Certified Public Accountants. They spent two days in discussion of accounting, auditing, and reporting problems.

This was the first occasion on which representatives of the two principal suppliers of financial information, management and auditors, confronted spokesmen for the two principal user groups, investors and credit grantors.

While there was diversity of opinion on the extent to which uniformity or comparability was possible or desirable, there was agreement on one important point—that the Accounting Principles Board was the only agency available in the private sector to promulgate authoritative accounting principles, and that it was eminently desirable to have the APB do this job.

Some participants suggested that management should have heavier representation on the Board, but the prevailing sentiment seemed to be that it would be preferable to have the Board principally made up of practitioners. This consensus was accompanied by expressions from management people, as well as the user groups, indicating a desire to have a voice at the earliest possible stage in the development of Board Opinions on specific accounting points.

The Accounting Principles Board had won its spurs.

To sum up, more than 30 years after the publication of the Institute's correspondence with the New York Stock Exchange and the enactment of the securities laws, there was still no authoritative, comprehensive code of accounting principles in existence.

However, many undesirable practices in corporate financial reporting had been eliminated, and far more disclosures of significance to investors had been required. Consistency from

period to period in the reporting of individual companies had been enforced.

The concepts of general acceptability and substantial authoritative support, as a basis for alternative accounting practices in similar circumstances, had been challenged, both from within the profession and without. These concepts had been challenged on two bases: one was that "the less desirable practices tended to drive out the preferable practices, somewhat as bad money drives out good"; and the other was that demands were growing for comparability among the statements of different corporations. These demands were a natural consequence of the growth in number of stockholders to approximately 25 million, and the rise of the financial analysts, whose business it was to advise investors on when to buy, sell or hold.

All informed observers conceded that absolute comparability was unattainable, in view of the judgmental factors inevitably required in the application of accounting principles. By its actions in 1964 and 1965, however, the Council of the Institute in effect declared that unnecessary obstacles to comparability should be eliminated. The SEC also, by its actions and utterances, was making it clear that reasonable comparability had become its objective.

By assuming greater responsibility and authority, the Institute, with increasing acceptance by management, bankers, and analysts, and with the encouragement of the SEC, offered the best hope of preserving the right of the private sector to develop the principles underlying corporate financial reports.

CHAPTER 7

Evolving Audit Responsibility

IN contrast with the turmoil in which statements on accounting principles were developed, the enunciation of authoritative guidelines for independent audits has been a steady, orderly process. One reason for this, no doubt, is that the extent and adequacy of their examinations are the responsibility of the accountants alone, whereas management, auditors, and regulatory bodies have shared responsibility for the representations made in financial statements. In the development of accounting principles, therefore, management, the stock exchanges, and the SEC, as well as the accounting profession, have had an influential voice.

Regulatory agencies, credit grantors, and investors, of course, have concerned themselves from time to time with the quality of independent audits, inasmuch as they added credibility to financial information on which important decisions were partly based. Generally speaking, however, these observers have been less interested in the techniques of auditing than in assurance

that audits resulted in financial statements on which they could rely with confidence.

The accounting profession has always been keenly aware of its responsibilities in the conduct of independent audits, and it has responded promptly to changes in the environment which indicated a need for extensions or refinements of auditing procedure.

In the early days of the profession in the United States, the accountants had nothing but precedent to guide them. There were no official statements on which to rely. It was in response to a need voiced by the Federal Trade Commission and the Federal Reserve Board that the first officially recommended audit procedures were prepared by the Institute in 1917, in the form of the famous Federal Reserve Bulletin, "Approved Methods for the Preparation of Balance Sheet Statements" (see Volume I of this work).

As mentioned in Chapter 2, revisions of this bulletin were issued in 1929, and again in 1936.

The existence of this 1936 revision, as indicated in Chapter 2, was of critical importance when the McKesson & Robbins case broke in 1938. It demonstrated to the public that the profession had not neglected its responsibility to establish authoritative guidelines for the conduct of independent audits. Without them the Securities and Exchange Commission might have found it necessary to fill the vacuum.

The McKesson case did result in the Institute's promulgation of "Extensions of Auditing Procedure," as noted in Chapter 2, requiring physical observation of inventories and confirmation of accounts receivable. This action made it unnecessary for the SEC to consider prescription of additional audit rules.

The committee on auditing procedure, which had developed "Extensions," was continued as a standing committee, parallel with the committee on accounting procedure, and it proceeded to issue a series of "Statements on Auditing Procedure" similar in form to the Accounting Research Bulletins.

However, the McKesson case had focused the attention of the SEC on auditing more sharply than before. William W.

Werntz, the chief accountant, in an address at the Institute's annual meeting in 1939 said: "In contrast to the time we have spent on accounting principles, there have been few cases before us involving the question of whether a reasonable audit was made."

He then discussed the underlying concepts of independent audits, the relative responsibility of management and the independent auditor, the competence with which audits were performed, the responsibility of the auditor for information contained both in financial statements and footnotes, and his responsibility for disclosures required in order to make such statements not misleading.

The question of competence, he said, included the extent of delegation to staff assistants, and the adequacy of supervision of their work. He also stressed the concept of independence which he defined as complete objectivity, freedom from bias, and avoidance of any entangling affiliation.

Mr. Werntz also discussed the conditions under which auditors were entitled to rely on systems of internal check and control—"to justify reliance, it is implicit that the auditor thoroughly inspect the system. . . ."

This speech led to the development of basic standards of auditing.

The Concept of Auditing "Standards"

After consultation with the Institute's committee on auditing procedure, the SEC suggested a distinction between auditing "standards," on the one hand, and auditing "procedures" necessary in the circumstances of a particular case to meet those standards. The Institute committee agreed. Recognizing that the distinction had not been clearly drawn in the official literature, the committee began the preparation of a statement on auditing standards. The work, however, was interrupted by more pressing requirements arising from World War II.

Meanwhile the SEC in 1941 issued Accounting Series Release No. 21, amending Regulation S-X, which required changes in the form of auditor's certificate, one of them being a statement as to whether "the audit was made in accordance with generally accepted auditing standards applicable in the circumstances."

The Institute's committee resumed the preparation of a statement on standards as soon as wartime pressures were relieved. In 1947 it published a special report, entitled "Tentative Statement of Auditing Standards—Their Generally Accepted Significance and Scope." Edward A. Kracke, a partner of Haskins & Sells, and a member of the committee on auditing procedure, was one of the principal authors of this statement. Mr. Kracke was a scholarly and articulate gentleman, dedicated to his profession, and he had labored diligently over successive drafts of this document.

The introduction began as follows:

> Auditing standards may be said to be differentiated from auditing procedures in that the latter relate to acts to be performed, whereas the former deal with measures of the quality of the performance of those acts, and the objectives to be attained in the employment of the procedures undertaken.

Acknowledging that it was on the initiative of the Securities and Exchange Commission that the representation as to standards was introduced in the accountant's report or certificate, the introduction stated that the distinction between standards and procedures therefore needed to be drawn with greater clarity in the official professional literature.

The tentative statement divided auditing standards into three broad categories:

General Standards

(1) The examination is to be performed by a person or persons having adequate technical training and proficiency as an auditor.

(2) In all matters relating to the assignment an independence in mental attitude is to be maintained by the auditor or auditors.

(3) Due professional care is to be exercised in the performance of the examination and the preparation of the report.

Standards of Field Work

(1) The work is to be adequately planned and assistants, if any, are to be properly supervised.

(2) There is to be a proper study and evaluation of the existing internal control as a basis for reliance thereon, and for the determination of the resultant extent of the tests to which auditing procedures are to be restricted.

(3) Sufficient, competent evidential matter is to be obtained through inspection, observation, inquiries, and confirmations to afford a reasonable basis for an opinion regarding the financial statements under examination.

Standards of Reporting

(1) The report shall state whether the financial statements are presented in accordance with generally accepted principles of accounting.

(2) The report shall state whether such principles have been consistently observed in the current period in relation to the preceding period.

(3) Informative disclosures in the financial statements are to be regarded as reasonably adequate unless otherwise stated in the report.

The text of the statement elaborated and explained these three types of standards. The document in its entirety occupied 43 printed pages.

In 1948 the membership of the Institute at the annual meeting approved the statement. The word "tentative" was then eliminated, and the original statement was supplanted by a booklet, "Generally Accepted Auditing Standards—Their Significance and Scope," which was issued as a special report of the committee on auditing procedure.

Procedural Guidelines

Up to 1948 the committee on auditing procedure had issued 22 formal statements on auditing procedure, seven of them

related directly to wartime conditions, but the remainder applicable to auditing generally.

In 1947 a note had been added to the basic bulletin, "Examination of Financial Statements by Independent Public Accountants," as follows:

> Parts of this bulletin, which was published in 1936, have been modified or superseded by the series of Statements on Auditing Procedure, now more than 20 in number, issued since 1939 by the American Institute of Accountants committee on auditing procedure.

A major addition to the official literature on auditing appeared in 1948. The committee had made a comprehensive study of internal control, and the results were published in a special report entitled "Internal Control—Elements of a Coordinated System and its Importance to Management and the Independent Public Accountant." This was a basic document, designed to aid auditors in the difficult decision as to how much reliance could be placed on clients' records and, consequently, the extent to which detailed checking could be curtailed.

At about the same time, the committee initiated a series of "audit guides," describing audits of special industries, such as securities brokers and dealers, the construction industry, and savings and loan associations.

The committee also sponsored case studies, published by the staff, illustrating audit procedures applied in actual examinations.

Altogether, this industrious committee on auditing procedure, in the decade between 1938 and 1948, under the chairmanship of three distinguished members of the profession—Samuel J. Broad, Paul Grady, and Alvin R. Jennings—made an impressive record of progress in the clarification of auditors' responsibilities.

This record was an example to successor committees, which sustained the effort with distinction. By 1969 the number of auditing statements had reached 41.

Certificates, Reports, Opinions

The representation which the auditor made as to the scope of his examination and his opinion on the financial statements —variously termed the auditor's certificate, report, or opinion —obviously had a direct relationship to the responsibility he assumed, and thus to his legal liability. As the responsibilities of auditors were clarified and extended over the years, the form of this representation underwent many changes.

The evolution of the auditor's report in the United States up to 1950 was described in a paper by George Cochrane, presented at the summer course of the Institute of Chartered Accountants in England and Wales, at Oxford University, and published in *The Accountant* (London), November 4, 1950.

Mr. Cochrane was the partner in charge of the United States practice of Deloitte, Plender, Griffiths & Co., one of the largest and best-known English accounting firms. He had been a member of the Institute committee which conducted the correspondence with the New York Stock Exchange in the early 1930's; he had also served as a Council member of the Institute, and as president of the New York State Society of Certified Public Accountants. In these capacities, and also as a member of the Institute's committee on accounting procedure, he had observed at first hand the developments of which he wrote in the Oxford paper.

In an introductory statement Mr. Cochrane said:

> Since accountancy as a profession was introduced into the United States of America by British accountants during the second half of the 19th century . . . the report which you [the British chartered accountants] used in those days was generally adopted, even though neither the American auditor's responsibility nor his duties had any statutory background. . . .
>
> The absence of statutory provisions requiring the issuance of accounts to stockholders, or the audit of accounts where they were required to be submitted, resulted in examinations which varied from a balance-sheet audit to a full detailed examination, although the auditor's report might be couched in the same words. . . .

The form of report, which Mr. Cochrane said was generally used from about 1900 until after World War I, read as follows:

> We have audited the books and accounts of the ABC Company for the year ended December 31, 1915, and we certify that, in our opinion, the above balance sheet correctly sets forth its position as at the termination of that year, and that the accompanying profit and loss account is correct.

The word "certify," Mr. Cochrane surmised, originated in an early English court decision in the *London and General Bank* case, in which it was stated that the auditor had to certify that the balance sheet was correct.

Since there existed no authoritative statement of acceptable accounting principles, and therefore no standard by which a reader could judge the "correctness" of the financial statements, this form of certificate left in doubt the auditor's basic responsibility, and exposed him to undefined liability. Accordingly, in cases in which auditors questioned accounting methods followed by clients, qualifications were inserted in the audit certificate, such as "subject to such and such" or "on the basis indicated." These practices in turn left readers in doubt as to the significance of the qualifying words.

Following issuance of the 1929 revision of the Federal Reserve Bulletin changes were made in the form of certificate generally used by the leading firms. Mr. Cochrane said that the usual form was as follows:

> We have examined the accounts of the ABC Company for the period from January 1 to December 31, 1929.
>
> We certify that the accompanying balance sheet and statement of profit and loss, in our opinion, set forth the financial condition of the company at December 31, 1929 and the results of operations for the period.

This report omitted reference to examination of the books and to "correctness" of the financial statements.

The decision of the New York Court of Appeals in the *Ultramares* case (see Volume I of this work, Chapter 14) re-

sulted in efforts to make it clear that the auditor's report was an "opinion," and not a guarantee. Accordingly, the word "certify" was eliminated. The form of report which then came into general use was:

> We have examined the accounts of the ABC Company for the year ended December 31, 1931. In our opinion the accompanying balance sheet and statement of profit and loss set forth the financial condition of the company at December 31, 1931, and the results of its operations for the year ended that date.

The Institute's correspondence with the New York Stock Exchange in the years 1932 to 1934 resulted in an entirely new approach to the accountant's report (see Volume I, Chapter 10). The objective was to make it clear that an auditor's examination consisted largely of testing and sampling, not a detailed check of all transactions, and that the auditor's representation was a professional opinion rather than a statement of fact. The concept of "accepted accounting principles" as a standard against which "fairness" of presentation could be measured was a sound innovation. The new affirmation of consistency in the application of accounting principles from year to year was also introduced. Furthermore, for the first time, the new form of report was recommended as a "standard" form, so that any deviation from its language would put the informed reader on notice that there was something unusual to be considered.

The new form of report, which was immediately widely adopted, was as follows:

> We have made an examination of the balance sheet of the XYZ Company as at December 31, 1933, and of the statement of income and surplus for the year 1933. In connection therewith, we examined or tested accounting records of the company and other supporting evidence and obtained information and explanations from officers and employees of the company; we also made a general review of the accounting methods and of the operating and income accounts for the year, but we did not make a detailed audit of the transactions.
>
> In our opinion, based upon such examination, the accompanying

balance sheet and related statement of income and surplus fairly present, in accordance with accepted principles of accounting consistently maintained by the company during the year under review, its position at December 31, 1933, and the results of its operations for the year.

Then came the Securities Acts with their new provisions relating to auditors' liabilities, and a few years later the McKesson case, resulting in the SEC's investigation of auditing procedures. As a result the Institute modified the standard short form of auditor's report, as follows:

We have examined the balance sheet of the ABC Company as of December 31, 1939, and the statements of income and surplus for the fiscal year then ended; have reviewed the system of internal control and the accounting procedures of the company, and, without making a detailed audit of the transactions, have examined or tested accounting records of the company and other supporting evidence by methods and to the extent we deemed appropriate.

In our opinion, the accompanying balance sheet and related statement of income and surplus present fairly the position of the ABC Company at December 31, 1939, and the results of its operations for the fiscal year, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

This report introduced the assertion that the system of internal control had been reviewed, implicitly justifying reliance on the system in lieu of detailed checking, to the extent deemed appropriate.

In 1941, as noted above, the SEC introduced the distinction between auditing standards and auditing procedures. Consequently the Institute recommended addition of the following words to the first paragraph in the standard form of report:

Our examination was made in accordance with generally accepted auditing standards applicable in the circumstances and included all procedures we considered necessary.

It was soon noted that, since auditing standards were of general application, the phrase "applicable in the circum-

stances" was inappropriate in this context. Accordingly this sentence was changed to read:

> Our examination was made in accordance with generally accepted auditing standards and included all procedures which we considered necessary in the circumstances.

In 1949, after years of experience and after the Institute membership had formally adopted the statement of auditing standards, a further revision of the form of report was approved, as follows:

> We have examined the balance sheet of ABC Company as of December 31, 1949, and the related statements of income and surplus for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.
>
> In our opinion, the accompanying balance sheet and statements of income and surplus present fairly the financial position of ABC Company at December 31, 1949, and the results of its operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

This form of report remained substantially unchanged to the time of this writing, except that the phrase "retained earnings" was later substituted for the word "surplus."

Influence of the SEC

The recommended form of auditor's report was intended, of course, to be used without qualification or exception only when the auditor had conducted his examination in accordance with accepted standards and had satisfied himself that the financial statements were fairly presented.

In cases in which limitations were placed on the scope of an auditor's examination, or in which the auditor had doubts

about conformity of the statements with accepted accounting principles, the language used in auditors' reports to reflect these facts varied widely among accounting firms. In some instances, such language was composed of what bankers called "weasel words."

Carman Blough, then chief accountant of the SEC, had discussed this problem in speeches delivered as early as 1936 and 1937. Among his comments were the following:

> It is not uncommon for an accountant to present financial statements and, in his certificate, point out certain facts of inclusion and exclusion without expressing any opinion as to whether the statements properly reflect the facts or not. . . . In our opinion, the protection of investors requires that the accountant who, by a narration of facts in his certificate, attempts to protect himself, should be required to express his opinion with regard to the propriety of showing the facts in the manner in which they have been shown.

Mr. Blough objected strongly to the phrase "subject to the foregoing," often used in the last paragraph of an auditor's certificate with reference to the preceding paragraph. "What is the meaning of this expression?" asked Mr. Blough. "Does it voice an exception or does it not? Some accountants who use the term say, 'No, we are not taking an exception; we are merely calling attention to the fact that the foregoing comments must be read in order to get an intelligent picture of the financial condition of the company or the results of its operations, but they are explanatory in nature and not qualifications.' Other accountants say, 'Most assuredly we intend to take exception. When we have stated a practice followed by the client and then say subject to the foregoing, we mean to say that our certificate is qualified by the matters previously recited.' If accountants cannot agree among themselves as to the meaning of this expression, how can investors be sure of the meaning intended?"

Mr. Blough also said, "Occasionally, an accountant seeks to protect himself by including in his certification numerous qualifications and exceptions. [This] leaves the reader with the feeling that there is more wrong than has been revealed."

Numerous qualifications and exceptions, he said, made it difficult to interpret the financial statements as a whole.

The Commission's first rule on certificates had provided that the accountant should state that he had, after reasonable investigation, reasonable grounds to believe, and did believe, that the statements were true, and that there was no omission of any material fact required to be stated therein or necessary to make the statements therein not misleading, except as specifically noted. This form followed closely the language of the statute.

After the Institute published the new form of report in 1934, this SEC rule was discarded. Its new rule read as follows:

> The certificate of the accountant or accountants shall be dated, shall be reasonably comprehensive as to the scope of the audit made, and shall state clearly the opinion of the accountant or accountants in respect of the financial statements and the accounting principles and procedures followed by the person or persons whose statements are furnished.

Mr. Blough noted that this provision, in effect, called for a certificate similar to the Institute's suggested form of report.

Reference has already been made to the 1939 speech by Mr. Werntz, who had then become the SEC's chief accountant, which led to the formulation of auditing standards. The Commission's first proposals for changes in the form of auditor's certificate to be incorporated in the amended Regulation S-X in 1941 were objectionable to the Institute in some respects, since they appeared to expose the auditor unfairly to extended liability. There were numerous conferences and much correspondence on this matter between the Institute's committee and representatives of the Commission. The Institute's counsel filed a brief supporting the Institute's position, in which they were joined by three other law firms representing accounting firms.

The committee reported in the spring of 1941 as follows:

> While the committee was not able, as a result of the various discussions and representations made, to obtain a favorable decision of

> the Commission on some questions raised, a number of changes were made in the proposed rule which were considered by the committee to constitute substantial improvements.

The Commission's new rules required that the accountant give a reasonably comprehensive description of the scope of the audit performed; and that if any generally recognized normal auditing procedure had been omitted with respect to significant items, such omission should be stated with a clear explanation of the reasons. Furthermore, it was required, as already noted, that the auditor state whether the audit was made in accordance with generally accepted auditing standards, as distinguished from detailed procedures. The Commission also added a requirement that appropriate consideration be given to the adequacy of the system of internal check and control. It was additionally required that exceptions be clearly identified, and to the extent practicable the effect of each exception on the related financial statements be given. Retroactive adjustments of the accounts of prior years were also required to be disclosed.

When "Extensions of Auditing Procedure" was first adopted by the Institute's membership, it was not required that omissions of the new procedures regarding inventories and receivables be disclosed if, in his judgment, the auditor found it not practicable or reasonable in the circumstances to undertake such procedures. The new SEC requirement that the omission of any normal procedures be disclosed in the auditor's report, however, applied a standard to listed companies differing from that applicable to others. Accordingly, the committee on auditing procedure recommended that disclosure be required in all cases in which the extended procedures regarding inventories and receivables were not carried out, regardless of whether they were practicable and reasonable, and even though the independent accountant may have satisfied himself by other methods. This recommendation was adopted.

Exceptions and Disclaimers

Statement on Auditing Procedure No. 1, "Extensions of Auditing Procedure," contained the following paragraph:

> The independent certified public accountant should not express the opinion that financial statements present fairly the position of the company and the results of its operations in conformity with generally accepted accounting principles, when his exceptions are such as to negative the opinion, or when the examination has been less in scope than he considers necessary. In such circumstances, the independent certified public accountant should limit his report to a statement of his findings and, if appropriate, his reasons for omitting an expression of opinion.

This pronouncement effectively eliminated expression of an opinion "subject to" some general statement in the auditor's report affecting material items, related either to specific accounting practices of the company—of which he might disapprove—or to limitations on the scope of his examination. No longer was it permissible, either, for an auditor to take specific exceptions with respect to material items in the financial statements, such as inventories or receivables, and express an opinion subject to those exceptions that the statements on the whole were fairly presented.

Even this requirement, however, left a loophole not immediately seen by the committee on auditing procedure.

The loophole was plugged, largely as a result of a one-man campaign conducted by Ira B. McGladrey of Cedar Rapids, Iowa, to whom reference was made in another context in Volume I of this work. Mr. McGladrey was a midwesterner of pioneer stock who had started a small accounting firm in Iowa some years after serving in the Army in World War I—a firm which later became the large regional firm of McGladrey, Hansen & Dunn. He was an independent thinker and a man devoted to high standards.

He pointed out to the Institute that it was still permissible

under the new rules for an auditor to state the scope of his examination, and withhold an opinion if his examination were limited or if he disagreed with a client's accounting principles —but without explaining to the reader the extent of the responsibility he did or did not assume. In long-form reports, issued in conjunction with financial statements intended for bank credit purposes, the audit procedures followed were frequently described but opinions of the auditors were omitted. The absence of an explanation of the extent of responsibility assumed by the auditor could be confusing or even misleading.

Mr. McGladrey proposed an additional requirement: that when an auditor could not properly express an opinion on the fairness of the statements as a whole, he should clearly disclaim an opinion and explain why—for example, that the audit was limited in scope, or that his exceptions as to accounting principles on material items made it impossible to state that the statements as a whole were fairly presented.

After discussions with Mr. McGladrey, the committee on auditing procedure was convinced that he was right. He was appointed a member of the committee in 1946.

In 1947 the committee issued Statement on Auditing Procedure No. 23, which, in effect, stated that when the auditor had not obtained sufficient competent evidence to form an opinion on the fairness of the statements as a whole, he should state in his report that he was unable to express an opinion on the statements and, in disclaiming an opinion, give all the substantive reasons for doing so. For example, when he disclaimed an opinion because the scope of examination was inadequate, he should also disclose any reservations or exceptions he might have regarding fairness of presentation.

Statement No. 23 was greeted with misgivings and even strong opposition in some quarters. A few state societies adopted resolutions opposing the statement.

Mr. McGladrey, Marquis G. Eaton, Alvin Jennings, then chairman of the committee on auditing procedure, and Carman Blough, then the Institute's director of research, explained the purpose of the statement at regional conferences and state

society meetings in various parts of the country during 1949 at which they found a good deal of misunderstanding.

Many practitioners believed that Statement No. 23 required a lengthy explanation of the omission of an opinion and the reasons why, even in cases where they prepared financial statements without audit and presented them on their stationery. Others were in doubt as to whether they could issue long-form reports at all, when they were not able to express an opinion on the overall fairness of the financial statements; still others were doubtful whether they could issue a qualified report in any case.

As a result certain amendments to Statement No. 23 were made before it was submitted for approval at an annual meeting of the Institute.

The restatement made it clear that an independent certified public accountant should not express the opinion that financial statements presented fairly a company's position and results of operations, in conformity with generally accepted accounting principles, when his exceptions were such as to negative the opinion, or when his examination had been less in scope than he considered necessary to express an opinion on the statements taken as a whole. In such circumstances the independent certified public accountant should state that he was not in a position to express an opinion on the financial statements taken as a whole, and should indicate his reasons therefor. To the extent that the scope of his examination and his findings justified, he could properly comment further as to compliance of the statements with generally accepted accounting principles in respects other than those which required the denial of an opinion on the overall fairness of the statements. The purpose of these assertions by the accountant was to indicate clearly the degree of responsibility he was taking.

The restatement further provided that whenever the accountant permitted his name to be associated with financial statements he should determine whether, in the particular circumstances, it was proper for him to (1) express an unqualified opinion or (2) express a qualified opinion or (3) disclaim an

opinion on the statements taken as a whole. Thus, when an unqualified opinion could not be expressed, the accountant must weigh the qualifications or exceptions to determine their significance. If they were not such as to negative the opinion, a properly qualified opinion would be satisfactory; if they were such as to negative an opinion on the statements taken as a whole, he should clearly disclaim such an opinion. His conclusions in this respect should be stated in writing, either in an informal manner, as in a letter of transmittal bound with the financial statements, or in the more conventional short-form or long-form report. However, when financial statements prepared without audit were presented on the accountant's stationery, without comment by the accountant, a warning, such as "prepared from the books without audit" appearing prominently on each page of the financial statements, was considered sufficient.

The amendments to the original statement, and the educational campaign undertaken in the meantime, effectively eliminated the opposition. Statement No. 23 was approved at a subsequent annual meeting, and thereafter the substance of the new requirement was incorporated in the Code of Professional Ethics by vote of the membership by mail ballot.

The success of these efforts to clarify the auditor's responsibility and make his report more informative won the applause of bankers, the SEC, and others concerned. The clients, for the most part, wanted their statements audited in accordance with the higher standards and were glad to pay additional fees, if necessary, to permit their CPAs to conduct examinations of sufficient scope to justify clean opinions.

Codification of Auditing Standards and Procedures

So many statements on auditing procedure had been issued in the intervening years that the 1936 revision of the Federal

Reserve Bulletin, "Examination of Financial Statements by Independent Public Accountants," was rapidly becoming obsolete. In 1946 this bulletin was withdrawn. In its place a pamphlet entitled "Audits by Certified Public Accountants" was published in 1950. Because of its red cover, this pamphlet was known as the "Red Book." Instead of presenting the elements of a specific audit program, the new publication contained 56 pages of explanation of the nature of financial statements, the significance of a CPA's report, underlying concepts of auditing, and typical auditing procedures.

Copies of the Red Book were sent to all members of the Institute and to the presidents of all commercial banks in the country. In addition, thousands of copies were sold. This new pamphlet was enormously popular. It served as a basis for discussions at meetings of state societies. The Robert Morris Associates, the national organization of bank credit officers, publicized it widely, and in a number of cities it was discussed in depth at joint meetings of bankers and CPAs. The committee on auditing procedure said in its report in the fall of 1950, "The response this booklet has received appears to indicate that it is filling a long-felt need for a brief statement describing the CPA's audit work."

Between 1950 and 1962, eight additional statements on auditing procedure were issued. At this point the committee on auditing procedure decided that an official codification of all currently effective pronouncements was needed. After months of intensive work, the committee produced Statement on Auditing Procedure No. 33, entitled "Auditing Standards and Procedures," with the unanimous affirmative vote of the 21 members of the committee.

This authoritative codification included the essence of the preceding Statements on Auditing Procedure relating to the responsibilities and functions of the independent auditor, generally accepted auditing standards and procedures, and reporting requirements. It became the bible for members of the profession as far as auditing was concerned.

Between 1962 and 1969, the committee on auditing pro-

cedure issued eight additional statements on auditing procedure, in addition to a special report on public warehouses. These bulletins dealt with long-term investments, letters for underwriters, inventory observation procedures, unaudited financial statements, working papers, reports following a pooling of interests, and subsequent discovery of facts existing at the date of the auditor's report.

Other documents dealing with auditing were also developed by other technical committees or the Institute staff, with supervision or clearance by the committee on auditing procedure: for example, *An Auditor's Approach to Statistical Sampling; Auditing and EDP;* "Audits of Banks"; "Audits of Brokers or Dealers in Securities"; "Audits of Construction Contractors"; "Audits of Fire and Casualty Insurance Companies"; "Audits of Savings and Loan Associations"; "Audits of Voluntary Health and Welfare Organizations"; and a "Medicare Audit Guide."

Compliance

It was one thing, of course, to publish standards and procedures, and another thing to see to it that they were generally applied in practice. Unlike many other professions, however, certified public accountants acting as independent auditors were exposed to wide public view. The pressures to comply with authoritative pronouncements were very great.

For one thing, generally accepted auditing standards and procedures, including reporting and disclosure requirements, were incorporated by reference in the codes of ethics of the Institute and of many state societies of certified public accountants.

A growing number of state boards of accountancy had also adopted similar codes. Accordingly, a CPA who failed to comply with the standards was liable to reprimand, suspension, or expulsion by his national and state professional societies, and

in many states was also liable to have his certificate suspended or revoked. Furthermore, accounting firms which served clients subject to the jurisdiction of the Securities and Exchange Commission were questioned by the SEC staff about any lapses from accepted standards which were visible on the face of the statements or the auditor's report. More seriously, such firms could be barred from certifying further statements subject to Commission review if trouble developed and the SEC found that there had been a material omission of accepted auditing procedure.

Banks and the courts were two additional sources of pressure for compliance with auditing standards.

The Disciplinary Machinery Works

An example of prompt and effective action by the profession's disciplinary authorities occurred in 1962 in relation to the widely publicized difficulties of Billie Sol Estes.

During the 1950's and early 1960's, the Department of Agriculture acquired record stocks of surplus grains. It adopted a policy of licensing privately owned warehouses—rather than government-owned facilities—for the storage of such grains.

Requirements for a federal warehouse license included adequate financial responsibility, which was determined by requiring statements of the warehouseman's net worth and adequate coverage under surety bonds.

In 1959 Estes' application for a federal warehouse license was approved, partly on the basis of a financial statement which later proved to show greatly inflated net worth, and a $200,000 surety bond. He rapidly expanded his grain-storage facilities.

In view of the greatly increased capacity of his grain-storage elevators, when the license came up for renewal in February 1961, the Agriculture Department required an increase in the surety bond and a "certified audit" of Estes' financial condition.

He presented financial statements bearing an opinion by an individual CPA residing in a Texas city far from the base of Estes' operations. According to the report of the Congressional subcommittee which investigated Estes' affairs, this CPA "actually made no audit; he received $6,000 for copying figures furnished by Estes on his letterhead."

Estes was arrested following an FBI investigation in 1962, and his empire collapsed, leaving creditors with losses of millions of dollars. His dealings with the government led to the Congressional investigation. Wide publicity was given to the case, and the financial statement bearing the opinion of the Texas CPA was prominently featured. *The Wall Street Journal* of May 23, 1962, for example, carried a story with the subhead, "Freeman Cites Public Policy; He Also Questions Ethics of CPA in Estes Audit." Actually, Orville Freeman, Secretary of Agriculture, had already submitted to the Texas State Board of Public Accountancy, and to the Institute, information bearing on the financial statements which the Texas CPA was supposed to have audited.

In a letter addressed to Billie Sol Estes, dated February 14, 1961, and signed by this CPA, the following statements were made:

> We have examined the balance sheet, presented in condensed form, of Billie Sol Estes as of December 31, 1960. Our examination was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances; except that our examination did not include the generally accepted auditing procedure of observing and testing the method used in determining inventory quantities, prices and amounts.
>
> By reason of the limitation of the scope of our examination as to inventories, no opinion may be expressed as to the fairness of presentation in the accompanying balance sheet of the financial position of Billie Sol Estes as of December 31, 1960.

The attached condensed balance sheet indicated net worth in excess of $13 million. Inventories were stated at approximately $942,000. The net worth was said to be greatly overstated.

Harsh things about the accounting profession were being said in the course of the Congressional investigation.

The American Institute immediately announced that it was conducting an investigation. Representatives of the Institute went to Texas to interview the accused member, and subsequently conferred with the state board, which was also making an investigation. It was learned that the CPA had actually not made an examination of Estes' books and records.

The CPA contended that since he expressed no opinion as to the fairness of the statements as a whole he had not violated any ethical standards. However, in a letter to the Secretary of Agriculture and congressmen involved in the investigation, the Institute's executive director stated:

> A key requirement is that the CPA's report should contain a clear-cut indication of the character of his examination, if any, and the degree of responsibility he is taking. . . . If the first part says that the auditor made an examination "in accordance with generally accepted auditing standards," as Mr. ___________'s report did, the reader is entitled to assume that the auditor tested underlying records and took other appropriate steps, except as otherwise noted, to enable him to form a judgment with respect to all important items in the financial statements. . . . In the present case a reader of Mr. ___________'s report would be reasonably entitled to assume that the auditor had done the necessary work with respect to all important items in the balance sheet so far as they were in no way connected with the inventory—for example, cash, securities, receivables, fixed assets, and liabilities. . . . Since the inventory in this case was comparatively small in relation to the other assets, a sophisticated reader might have wondered why it was necessary for the auditor to refuse an opinion on the statement as a whole. . . . However, this would not excuse an auditor for saying that he had made an examination in accordance with accepted auditing standards if, in fact, he had not made such an examination, or for failing to state clearly his reasons for being unable to express an opinion on the statement as a whole, if, in fact, there were important reasons other than those mentioned.

This letter was quoted by the Secretary of Agriculture in testimony before a Senate committee involved in the investigations.

The Texas CPA's certificate was suspended by the Texas State Board of Public Accountancy and his membership in the Institute was immediately terminated by the executive committee under a bylaw provision permitting such action when a member's CPA certificate had been withdrawn.

No change in auditing standards or procedures was indicated by this case. The facts indicated simply noncompliance with the standards. The Institute's prompt investigation of the matter, and the equally prompt action of the Texas state board, diverted any further unfavorable publicity, which probably would have mounted in intensity as the investigation proceeded.

Many less prominent and less dramatic cases of substandard auditing or reporting were dealt with by the profession's disciplinary authorities as a matter of routine.

Influence of the Banks

Informally and quietly the banks also served as a check on substandard auditing. While no bank admitted that it blacklisted accounting firms whose work was not up to standard, it was no secret that bankers used discreet influence to persuade prospective borrowers to have their audits conducted by accounting firms which were known to be reliable.

The Robert Morris Associates distributed to its members a constant flow of material related to auditing standards and procedures. In this it was encouraged by the Institute, whose committees collaborated with Robert Morris committees in the preparation of pamphlets and brochures which would help bankers to judge whether financial statements offered to them for credit purposes were up to standards.

These co-operative activities were broadened in 1966 when a National Conference of Bankers and Certified Public Accountants was organized at the suggestion of the president of the American Bankers Association, which represented more

than 15,000 commercial banks throughout the country. The Conference consisted of representatives of the Institute and of the American Bankers Association, some of whom were also members of the Robert Morris Associates. This group held a series of meetings at which current problems of mutual interest were discussed. The conclusions were published in brochures which were widely distributed among bankers. The first was a booklet on "The Auditor's Report: Its Meaning and Significance"; the second was on "Financial Statement Provisions in Term-Loan Agreements."

Efforts were also made to encourage bankers to report to the state societies or the Institute cases in which they suspected that substandard auditing had occurred. For legal reasons, however, it seemed impossible to work out satisfactory arrangements for this purpose.

The Practice Review Committee

The Institute recognized that bankers and other outsiders would hesitate to file complaints which might result in disciplinary action against CPAs. Accordingly it was decided to create a "practice review committee" which was charged not to disclose to the ethics committee any information which it received.

This committee invited bankers and others interested to submit reports of CPAs which raised questions as to whether auditing and reporting requirements had been properly observed. Assurance was given that no disciplinary action would result. Furthermore, the committee expressed no opinion to the persons who submitted such reports. It communicated only with the member who had issued the report, pointing out any apparent failures to comply with accepted standards.

The practice review committee issued two bulletins, in 1966 and 1968, which were sent to all members of the Institute engaged in public accounting practice. These bulletins indicated the nature of cases in which failure to comply with the

standards had been discovered. By providing members with these examples, it was hoped that other members would avoid similar errors.

Influence of the Courts

The legal sanctions to which all professions are subject also constitute a powerful pressure on practitioners to comply with authoritative standards. Litigation occasionally also discloses specific situations to which no existing standards are applicable. In such cases, judges or juries can make decisions which, having the force of legal precedent, may thrust new standards on the profession.

For the most part, the accounting profession in the United States has averted the imposition of standards by the courts. This has been accomplished either by issuing authoritative pronouncements before the questions involved were raised in litigation or by plugging gaps disclosed in litigation, through official pronouncements issued promptly enough to acquire authority before a legal precedent became firmly established.

There have been relatively few court decisions affecting auditing in the United States, as contrasted with the massive case law on the subject in the British Commonwealth, though some of the few American cases have been widely publicized.

As mentioned previously, a few lawsuits against prominent accounting firms, involving well-known corporations, occurred in the mid-1960's, and were the subject of much public comment. Since at the time of this writing the end results were not known, any attempt to analyze the facts and draw conclusions here would be inappropriate.

Of fundamental importance is the basic legal principle that the standard of performance to which a professional man is held under common law is that standard which may reasonably be expected of his peers. This general principle was repeated in a widely publicized case in 1968, in which the court said,

"Accountants should not be held to a standard higher than that recognized in their profession."

Authoritative statements by a professional body, such as the American Institute of Certified Public Accountants, are acceptable as evidence in court, and generally speaking are likely to outweigh the testimony of individual experts. Compliance with standards promulgated by a recognized professional body is therefore a strong defense against unjustified claims. By the same token, failure to comply is dangerous.

This was brought out in 1965 in a case in which an accountant who was not a member of the Institute was nevertheless held liable for failure to conform with standards which the Institute had published.

The court held that a CPA firm, which, without a disclaimer, presented on its stationery an unaudited balance sheet containing substantial errors, could not avoid liability for negligence by claiming that the statement "merely purported to reflect the condition of plaintiff's books."

The court found that the defendants' failure to place any qualification notice on the balance sheet clearly constituted a violation of the applicable rule promulgated by the Institute "which, without any doubt, fixes the existing and accepted standards of their profession."

Another case involved forged warehouse receipts which were used as a basis for loans. The circumstances were extremely complicated. The committee on auditing procedure undertook an exhaustive study of controls and safeguards applicable to field warehousing and to the issuance of warehouse receipts which banks accepted as collateral for loans.

The resulting 15-page special report, "Public Warehouses—Controls and Auditing Procedures for Goods Held," recommended that the independent auditor of a warehouseman study and evaluate the effectiveness of both accounting controls and administrative controls relating to accountability for and the custody of all goods placed in the warehouse; test the warehouseman's records relating to accountability for all goods placed in his custody; test the warehouseman's accountability

under recorded outstanding warehouse receipts; observe physical counts of the goods wherever practicable and reasonable; reconcile tests of such counts with records of goods stored; and confirm accountability, to the extent considered necessary, by direct communication with the holders of warehouse receipts.

The independent auditor was warned to apply such other procedures as he considered necessary in the circumstances. A portion of the bulletin was also directed to the warehouseman himself, with regard to internal controls, the receipt, storage and delivery of goods, and the control of warehouse receipts.

Thus another gap was plugged, so to speak, in the official literature on auditing standards and procedures. The incident illustrated the impossibility of predicting in advance all types of situations, in all the varied types of industries, in which established audit procedures might not disclose material facts of concern to creditors or investors.

In another widely discussed case, an important question arose as to the auditor's responsibility to disclose errors in financial statements on which he had already expressed an unqualified opinion, but which he was asserted to have discovered later, between annual audits. Even though the errors were corrected in the subsequent annual audit, it was contended that they should have been disclosed at the time of discovery.

The official literature was silent on this point. The committee on auditing procedure made an intensive study of this difficult question in conjunction with legal counsel. The result was Statement on Auditing Procedure No. 41, "Subsequent Discovery of Facts Existing at the Date of the Auditor's Report," issued in 1969.

This bulletin provided guidance—which of course was unavailable to the defendants in the case which prompted it—to CPAs encountering similar situations, and provided those who complied with it a defense against unjust claims.

In still another case, the trial judge suggested that the

American Institute of Certified Public Accountants and the Securities and Exchange Commission should revise auditing standards and accounting principles to cover cases of the kind before him: "That would be the way . . . to protect the public from this type of risk."

Protection Against Unjust Claims

Before World War II, a number of claims against accountants were made by surety companies because of the accountants' failure to detect defalcations or other irregularities. In these cases the client was protected by a fidelity bond and was indemnified by the surety company which issued the bond. The surety company, being subrogated to whatever claims the client might have had against the accountants, would sometimes attempt to bring a suit asserting negligence by the accountants.

Despite repeated public declarations by the Institute that the sampling and testing process, however carefully it was conducted, would not necessarily disclose all irregularities, suits of this nature continued. As a result, the Institute entered into discussions with leading surety companies in the early 1940's. It was pointed out that auditors commonly recommended to their clients the purchase of adequate fidelity bond coverage. The surety companies were paid adequate premiums for this protection. The auditors, on the other hand, had announced officially that their examinations were based on testing and sampling procedures which would not disclose all irregularities, and their fees were therefore less than they would have to be if they were expected to extend their examinations to the extent necessary to detect such irregularities. It was argued that it was unfair for accountants to be the object of claims by surety companies which had been paid for protection against losses which the accountants had not been paid to discover.

The force of this argument was persuasive. Accordingly a number of the most prominent surety companies entered into an agreement with the Institute not to bring such claims against accountants except in cases where an impartial committee found evidence of affirmatively dishonest or criminal acts or gross negligence on the part of accountants. This agreement was entered into in 1945, and in subsequent years a number of additional surety companies subscribed to it. Some later withdrew, but in a number of cases the agreement forestalled claims against accountants, and it resulted in informal settlement of others.

The Institute attempted to protect its members against unjust claims from any source by engaging counsel to keep track of all litigation against accountants, by offering to provide expert testimony on behalf of members against whom claims were filed which the Institute believed were ill-founded, and by filing briefs as friend of the court in cases which presented questions of potential importance to the profession at large.

Over the years the Institute also negotiated with insurance companies in an effort to assure that adequate liability insurance would be available to its members, and periodically notified its members of the desirability of carrying adequate coverage of this type.

In retrospect, it seems fair to say that, while the organized accounting profession has tried to protect its members against unfair penalties, it has also done everything within its power to clarify the responsibilities of auditors, and to improve the quality of independent auditing and reporting. The results have been good. Independent audits in the United States improved greatly in the 30-year period from 1938 to 1969.

No doubt, much more remains to be done. The development of professional standards will always be an evolutionary process. As the environment changes it will be necessary continually to review, extend, and codify auditing procedures in order to better serve the public interest.

CHAPTER 8

The Concept of Independence

FOR decades, the phrase "independent audit" has been used to describe the "outside" review of management's financial statements, and the person who conducts such a review has been called the "independent auditor."

The word "independent," however, has various shades of meaning, and the concept of independence, as it applies to certified public accountants in their capacity as auditors, has become over the years complex and somewhat elusive.

It seems probable that the term "independent auditor" was first used in the sense of independent contractor—to distinguish the auditor offering his services to the public generally from an auditor employed by a company. The word "independence," as professional accountants came to apply it to themselves, was generally assumed to mean integrity, honesty, and objectivity.

Independence was regarded as a state of mind and a matter of character. Leaders of the profession constantly reminded their colleagues that they must not subordinate their judgments to those of their clients. Otherwise, obviously, audits by CPAs would be little more than a check of arithmetical accuracy.

So familiar was this concept of independence within the

profession that it did not seem necessary to deal with it formally in the Code of Professional Ethics. To state that an auditor must be independent would have seemed as unnecessary as to state that he must be honest.

The "Appearance" of Independence

In 1932, however, it began to dawn on a few CPAs that silence on the subject of independence might not be sufficiently reassuring to the public. Just before enactment of the Securities Act of 1933, the chairman of the Institute's ethics committee proposed, as noted in Volume I of this book, that a rule be adopted prohibiting members of the Institute from being officers or directors of corporations which they served as independent auditors. While there was some support for this proposal in the Council—indeed, it was even suggested that the proposed rule be extended to prohibit a financial interest in a client corporation—the majority of the Council rejected it as unnecessary. No doubt, the general feeling was that an auditor could be just as honest and just as objective whether he served on the board of directors or owned stock in the client company or whether he didn't. But the fact that the proposal was made showed that some of the leadership was becoming conscious of a need to preserve the *appearance* of independence, as well as independence in fact.

After the enactment of the securities legislation, the SEC promulgated rules providing, among other things, that accountants would not be considered independent if they had relations with clients which might subconsciously impair their objectivity. Specifically it was provided that an accountant would not be *considered* independent by the Commission if he were an officer or director of the client, or if he had a substantial financial interest in the enterprise.

Thus the element of appearance, in addition to the element

of actuality, was officially introduced into the concept of independence as it applied to the accounting profession.

It was not until 1941, however, that the Institute introduced a similar prohibition into its own rules of professional conduct. The new rule provided, in effect, that a member auditing the accounts of an enterprise financed in whole or in part by public distribution of securities could not be the actual or beneficial owner of a substantial financial interest in the enterprise; however, in the case of a company not financed in part or in whole by the public distribution of securities, but whose statements were to be used as a basis of credit, the rule provided that a member could audit the accounts and still have a substantial financial interest in the enterprise if he disclosed such interest in his report.

This was a partial acquiescence in the SEC's precedent. Members of the Institute auditing publicly held companies were subject to the SEC's rule in any case.

The only thing the Institute added was the requirement that an auditor of a closely-held company who had a substantial financial interest in the enterprise must disclose it. Even at this time no prohibition against service as auditor and also officer or director of a client company was included in the rule, despite the fact that the SEC had forbidden it for almost a decade.

Meanwhile, the SEC had begun to issue releases describing specific cases under its general rule in which individual accountants had been found to be not independent. The first of these was Accounting Series Release No. 2, dated May 6, 1937, in which it was held that an accountant was not independent because he held stock in a client corporation, the value of which constituted more than one per cent of his personal fortune.

This was the first definition of the word "substantial" in the context, and it aroused indignation among some members of the accounting profession. They resented the presumed implication that a CPA's professional judgment might be improperly affected by an insignificant financial interest. They

still equated independence with integrity, and a challenge to one seemed a reflection on the other.

However, in due course the Institute amended its own rule so as to prohibit, in the case of publicly held companies, a financial interest "substantial either in relation to its capital or to his own personal fortune." The rule continued to require disclosure in the case of financial statements used as a basis of credit if the auditor owned a financial interest of the same magnitude. However, the Institute pointedly refrained from setting a percentage limitation on the value of such financial interest.

In 1944 the SEC, in Accounting Series Release No. 47, listed and summarized 20 rulings on accountants' independence in specific cases. These ranged from fairly clear-cut situations—in one an employee of the accounting firm concerned was the controller of the registrant corporation; in another the accountant clearly subordinated his judgment to that of the client—to other situations where it was not so clear that the relationships were likely to impair independence.

For example, in one case an accounting firm was considered not independent by the SEC because one of its employees did much of the bookkeeping of the registrant. The Institute's committees on ethics and on auditing procedure disagreed. Their conclusion was stated in a report of the committee on auditing procedure to the Council, as follows:

> Both committees were in agreement that if an accountant is in fact independent, and if he has performed all the auditing procedures necessary to supplement the information obtained through keeping the books, he should be entitled to express any opinion he may have formed. However, there was some uncertainty as to whether the two committees were in agreement regarding whether the accountant should disclose in his report the fact that he had kept the books. After further consideration the committees have agreed that this is a question which should be left to the judgment of the accountant in the light of the facts of each case. The committees believe that disclosure of the fact that he has kept the books is not usually necessary.

Independence "in Fact"

There is no doubt that the profession warmly embraced the concept of independence *in fact*. It received great emphasis in the "Tentative Statement of Auditing Standards" promulgated in 1947. Under the heading, "Independence in the Auditor's Mental Attitude and Approach," the statement said:

> There is probably no concept relating to the professional auditor that is today in greater need of elucidation than that of his "independence" as that term is widely used. In the profession's early days, "hanging out his own shingle" sufficed for an outward mark of independence, while the literature of his profession taught the simple virtue of complete intellectual honesty as its essence. But progress brought problems, and one of them in the auditor's realm was how the attribute of complete intellectual honesty might be recognized as something additional to the fact of his being engaged in professional public practice. So there arose a quest for signs—signs by which any lack of independence might be recognized.
>
> . . . The profession has gradually compiled . . . precepts and conditions to guard against the *presumption* of loss of independence. "Presumption" is stressed because insofar as intrinsic independence is synonymous with mental integrity, its possession is a matter of personal quality rather than of rules that formulate certain objective tests.

The statement then cited five of the Institute's rules of professional conduct designed to guard against the presumption of loss of independence: the rules on false or misleading statements, contingent fees, financial interest in a client's business, commissions and brokerage from the laity, and occupations incompatible with public accounting. The statement continued:

> Independence in the last analysis bespeaks an honest disinterestedness on the part of the auditor in the formulation and expression of his opinion, which means unbiased judgment and objective consideration of facts as the determinants of that opinion. It implies not the attitude of a prosecutor, but a judicial impartiality that recognizes an obligation on his part for a fair presentation of facts which he owes not only to the management and the owners of the business. . .

> but also to the creditors of the business, and to those who may otherwise have a right to rely (in part, at least) upon the auditor's report, as in the case of prospective owners or creditors.

The spokesmen for the profession were concerned by the tendency of the SEC to specify an increasing number of relationships which would result in an accountant's being *considered* not independent—regardless of whether or not he was independent in fact. They were reluctant to impose on themselves rules against various relationships which might suggest to some observers a lack of independence, even though the accountant concerned was the soul of integrity and objectivity.

Even the rule against financial interest in a client's business had met with some resistance, despite the fact that the SEC had already established it. Some accountants argued that they did not lose their integrity because they held a few shares of stock in a client company. And, of course, no one was accusing them of losing integrity in such a case. The point was, what would other people think—what would the public think?

The SEC, at any rate, was protecting itself by not accepting "certificates" from auditors whose relations with clients would appear to the public to create conflicts of interest.

In the old days it was not unusual for an accountant to accept his fee in stock, particularly if the client was trying to get established or was temporarily short of cash. Until the SEC came along, there was no prohibition against serving both as auditor and as a director of a client company, and this, too, was not infrequently done. After all, directors were supposed to represent the stockholders, and the auditors, too, recognized a responsibility to report fairly to stockholders. Indeed, when the Institute finally amended its rule to prohibit joint service as auditor and director, many years after the SEC had prohibited it, some English chartered accountants expressed surprise and concern that their American colleagues would thus limit their opportunities for service, and by the mere acceptance of such a limitation permit the inference that their integrity might be impaired by the dual relationship.

The Council Speaks

The growing concern in the United States about the questions on independence raised by the SEC, and its rulings in specific situations, was evidenced in a statement adopted by the Council of the Institute in 1947—the same year in which the "Tentative Statement of Auditing Standards" was released.

The principal author of the statement adopted by the Council was Samuel J. Broad, who had served as chairman of the committee on auditing procedure, and as president of the Institute in 1944-45. He was one of the most thoughtful students of the auditor's role.

This rather lengthy statement began by tracing the development of the demand for independent audits, and continued, "In the field of auditing, the certified public accountant is under a responsibility peculiar to his profession, and that is to maintain strict independence of attitude and judgment in planning and conducting his examination and in expressing his opinion on financial statements."

Outlining the evolution of the independent audit in England, the statement continued, "Historically, independence was the first requirement; the need for that was recognized even before the need for technical competence; it was the climate into which the profession was born."

Referring to the changes in the American economy in recent decades, the statement described the expanding scope of the CPA's services, including accounting assistance and advice to business management in the installation of accounting and cost systems, budgeting, internal control, and other fields of methods and procedures. The great demand for the services of accountants in tax practice was also mentioned.

". . . The maintenance of mutual confidence which is necessary in business relationships and transactions," was emphasized as an important function of the CPA. "With the growth of business enterprises the public accountant makes a vital contribution in meeting the need for independent, impartial, and expert opinion on the financial position and the results

of operation. This is his unique contribution, a service which no one else offers or is qualified to perform."

Reference was made to the Institute's rules of conduct designed to insure independence, and to the SEC rules prohibiting service by the auditor as a director, officer, or employee of the client company.

The need for professional judgment was emphasized, and it was stressed that the independent accountant should conduct his examination in accordance with accepted standards, regardless of limitations of time or fee.

In other phases of his work, such as tax practice, it was said that the CPA's function was to prepare or assist the client in preparing and presenting required information. Here the decisions were not his, but those of the parties at interest. However, "He should not distort the facts or omit to state any material fact known to him which is required by the prescribed forms or is requested by the interested parties."

The statement concluded: "Rules of conduct can only deal with objective standards and cannot assure independence. Independence is an attitude of mind, much deeper than the surface display of visible standards. These standards may change or become more exacting, but the quality itself remains unchanged. Independence, both historically and philosophically, is the foundation of the public accounting profession and upon its maintenance depends the profession's strength and its stature."

Tighter Rules by SEC, Illinois, New York

This statement was a useful declaration of policy and no doubt had a strong influence on members of the profession. It did not, however, prevent the SEC from tightening its specific rules related to independence. In December 1950, the Commission amended provisions of Regulation S-X in a number of respects. One change was the omission of the word

"substantial" from the provision regarding financial interests of accountants in client businesses. As amended the pertinent sentence read as follows: "For example, an accountant will not be considered independent with respect to any person, or any affiliate thereof, in whom he has *any* financial interest, direct or indirect, or with whom he is, or was during the period of report, connected as a promoter, underwriter, voting trustee, director, officer, or employee" (emphasis supplied).

It was understood that this change was made because the Commission was tired of having arguments about what constituted a "substantial" financial interest. The previous ruling, that more than one per cent of an accountant's personal fortune would be regarded as substantial, left open the question why one and one-tenth per cent, even though a small amount of money, was substantial, while nine-tenths of one per cent was not substantial, even though it might amount to a large amount of money in absolute terms.

In 1954 the Illinois Society of Certified Public Accountants adopted a new rule of ethics prohibiting a member, or a firm of which a member was a partner, from expressing an opinion on the financial statements of any organization if the member, his partners, or their immediate families living in the same household, had a direct or indirect financial interest in the organization in question. This in effect affirmed the SEC's position, ignoring the distinction in the Institute's rule between clients whose securities were widely distributed and clients whose statements were used for credit purposes, as well as the distinction between "substantial" financial interest and "any" financial interest.

Some dissatisfaction with the new Illinois rule was expressed, both in the Institute and in Illinois, and at least one prominent member resigned from the Illinois society because of it. As it turned out, however, the Illinois society showed foresight. The Institute was to follow its example some years later—not without travail, as will be explained shortly. It was difficult to justify a double standard of independence, one for the SEC and another for companies not subject to its

jurisdiction. In the latter category, mere disclosure of a financial interest, as the Institute required, was not likely to be reassuring to third-party users of financial statements, who could hardly be expected to appraise the significance of the disclosure.

The New York State Society of Certified Public Accountants had also taken a step beyond the requirements of the Institute. It had adopted a rule prohibiting joint service as auditor and employee or director of an enterprise unless such relationship was disclosed in the auditor's report.

In 1959, Andrew Barr, chief accountant of the SEC, made a speech before the Ohio State University Institute on Accounting which attracted much attention.

Mr. Barr's name has been mentioned on a number of occasions previously in this narrative, but without adequate background. He was a CPA, a member of the Institute, and a member of its special committee on research program (see Chapter 6). He had had experience in public accounting, had taught accounting at universities, and had served on the SEC's staff before becoming chief accountant. He was a combat officer in World War II. His technical competence, his judicial approach, and his sincerity won the respect of the profession as a whole. The Commission depended on him for advice on accounting matters, and his quiet influence on policy was often evident.

In his Ohio speech Mr. Barr reviewed the evolution of the independence concept, both before and after enactment of the Securities Act. He referred specifically to the "double standard" in the profession's ethical code—"permitting no substantial interest in a client with public distribution of securities, but only requiring disclosure of such an interest to private lenders." He cautiously suggested also that the code might be strengthened by prohibiting joint service as auditor and officer or director of the client.

"Any course of conduct by the profession which may have the effect of undermining public confidence in the independence of accountants," Mr. Barr said, "would destroy the useful-

ness of the accountant's work in the securities field. It is for this reason that the SEC has vigilantly guarded the concept of independence—so firmly in some cases as to bring criticism from the properly constituted guardians of the profession's code of ethics. . . . I know that our intent has been to promote the highest standards in one of the most important qualities of the accountant in public practice."

This speech did not go unnoticed by the Institute's committee on professional ethics.

Facing Up to the Issue

It had become quite clear to that committee that the Institute's rule was obsolete, embarrassing, and possibly harmful to the smaller accounting firms. The rule permitted joint service as auditor and officer or director, and permitted auditors of closely held companies to have a financial interest in such companies, provided it was disclosed, while auditors of publicly financed corporations were not permitted either course of action by the SEC.

The Institute was indeed maintaining a double standard, which not only gave the impression of philosophical schizophrenia, but possibly suggested to outsiders a double standard of behavior in actual practice.

The possession of a financial interest by a CPA in a client of which he was independent auditor either did create an appearance of lack of independence, or it did not. If it did not, the proper posture for the Institute would have been to oppose the SEC's rule, and refuse to affirm it. If such a financial interest did create the appearance of a lack of independence, then it could not be helpful to smaller accounting firms for the Institute to encourage an assumption that they were less independent than the larger firms which audited publicly financed corporations. The same line of argument was applicable to service as officer or director of an audit client.

Off-the-record comments by metropolitan bankers indicated uneasiness about the close relations of some local accounting firms with their clients. Such uneasiness could only be heightened by the knowledge that some local firms owned stock in their client's enterprises, or participated in the management. It was surmised that this uneasiness might well influence big-city bankers, not personally acquainted with the smaller firms concerned, to encourage borrowers to change accountants—to engage firms that were subject to the stricter SEC rules in the belief that they would afford greater protection to the credit grantors.

In the spring of 1960, the Institute's committee on professional ethics proposed to the Council amendment of the rules of conduct so as to prohibit any member from having any financial interest in an enterprise for which he acted as auditor, or from serving as employee or director of such an enterprise. After lively debate, and in spite of strong opposition, a substantial majority of the Council voted in favor of this proposal and recommended its adoption by the membership. It was put on the agenda for discussion at the following annual meeting to be held in Philadelphia in September 1960.

At the next Council meeting, immediately preceding that annual meeting, an effort was made to have the Council withdraw this recommendation. It was urged that the amendment would work a hardship on many local practitioners who had minor financial interests in client enterprises or served on their boards. However, a motion to withdraw the recommendation was put to a vote and defeated.

Two days later, at the annual meeting of the members, a discussion of the proposed amendment took place which can only be described as a Donnybrook.

The formal proposition was that the existing Rule No. 13 be deleted, and that a new rule be substituted for it, which in substance provided that a member should not express an opinion on financial statements of an enterprise unless he and his firm were in fact independent with respect to such enterprise; that independence was not susceptible of precise defi-

nition, but was an expression of the professional integrity of the individual; that the member had the responsibility of assessing his relationships to determine whether he might expect his opinion to be considered independent, objective, and unbiased by one who had knowledge of all the facts; but that a member would not be considered independent with respect to any enterprise if he or any of his partners during the period of the professional engagement or at the time of expressing his opinion had, or was committed to acquire, any direct financial interest, or material indirect financial interest in the enterprise, or was connected with the enterprise as a promoter, underwriter, voting trustee, director, officer, or key employee. An exception was made with respect to directorships of charitable, religious, civic, or other similar types of nonprofit organizations when the duties performed in such capacity were such as to make it clear that the member could express an independent opinion on the financial statements.

Thomas G. Higgins, chairman of the committee on professional ethics, who was senior partner of Arthur Young & Company, presented the matter for discussion. He conceded its controversial nature, but contended that it was the most important matter before the ethics committee during the past five years—as important, in his opinion, as Statement on Auditing Procedure No. 23, and as important as the profession's decision many years ago not to advertise, both of which had also involved much controversy. He reminded the audience that if the members present at the annual meeting approved submission of the new rule to a vote by mail ballot of all the members of the Institute, the vast majority who were not present would have an opportunity to express their views.

The practical effect of the proposal, Mr. Higgins said, would be to preclude an Institute member from expressing an opinion on financial statements if he were connected with the client either by holding such a position as director or officer, or by having a direct financial interest or a material indirect financial interest in the enterprise. He pointed out that the proposed rule was virtually the same as that adopted by the Illinois

society six years before, and virtually the same as the existing SEC rule.

Mr. Higgins stated four main reasons why the proposed rule would be beneficial to the profession. First, he said there was a pressing need for some general statement of the Institute's concept of independence: "For years the concept of independence has been the foundation stone of our ethical concept, and yet the word 'independence' appears nowhere in the formal rules of conduct." Next, he said there was need for a uniform standard of independence—it made little sense that there should be two standards. Third, he contended that the proposed rule would be helpful to all practitioners: the financial public would be aware that every member was required to adhere to the same exacting rule as all other members. The real question, he said, was not so much the absence or presence of independence in fact, but how third parties having knowledge of the circumstances would react to the situation.

Finally, he referred to the increasing focus of nationwide attention on conflicts of interest and standards of conduct in public life: it seemed unlikely that any institution, including the accounting profession, would escape scrutiny. The Institute, he said, should provide leadership by taking a definite stand. He expressed the view that there could not be a bigger boost for the accounting profession's public relations than newspaper reports that its national organization had taken a positive stand against conflicts of interest.

Following Mr. Higgins' remarks, a motion was made that the proposed rule be approved for submission to the entire membership for a vote by mail ballot.

Violent opposition was expressed. One speaker insisted that the word "integrity" covered the situation adequately and that it was unnecessary to make specific rules about independence.

Another member conveyed a resolution adopted by a state society, to the effect that the proposed rule would impugn the professional stature of the CPA and would be an effort to legislate morality; further, that it was often in the best interests of a community, or a client, for a CPA to own a small

number of shares of stock in a client corporation. This state society recommended that the proposed amendment be defeated.

Questions were raised as to the meaning of "material indirect financial interest."

The proposal was attacked on the ground that the proposed amendment would impose undue hardship on many practitioners and would weaken many client relationships developed over the years: where directorships or minor offices in client enterprises were accepted as a matter of convenience, and independence in fact was not impaired, there was no valid reason why such offices should have to be surrendered.

One member said, "I don't think we should be compared to a judge on a bench who hears both sides of the case, and I don't think we should be compared to an officer of New York City who has taken bribes." This remark evoked applause.

On the other hand, there was no lack of support for the amendment.

One speaker argued that in fact the position of the independent auditor *was* comparable to that of a judge. He asked whether anyone would care to sue a corporation before a judge who happened to be on the board of directors.

Other speakers said the main issue was what the public might think, rather than whether accountants actually acted with integrity or not.

Another member pointed out that the profession was growing rapidly: "We are all very proud of our accomplishments, but it seems to me that as we grow in numbers we should grow in stature. . . . I honestly don't see how this organization can put their own selfish interests and the way it affects their own individual practices in front of the good of the profession as a whole." These remarks also evoked applause. The speaker referred to the present controversy as one of the profession's growing pains, and compared it with the lengthy debate some years before over Statement on Auditing Procedure No. 23: "I am positive that if we adopt this rule on independence, a few years from now as we look back we wouldn't want to go back and put ourselves in the position we were in before adoption."

Still another speaker said, "If you refuse to vote this rule, you will place upon this profession one of the worst blots that has ever been placed upon it." He referred to the growing public concern with conflicts of interest in business and government: "The question here is, we have to show the public by our actions that they have a right to put their confidence in us."

Emotional tension mounted. A motion to table the pending motion was seconded, but upon being put to a vote was defeated. Members stood up in various parts of the room, calling for the floor, and raising points of order.

A suggestion that a straw vote be taken was shouted down.

It was moved that action on the question be deferred. This motion was seconded.

After further discussion, the question was called for.

A motion was made that proxy votes not be permitted. This was ruled out of order.

After more discussion, it was finally ruled that proxies could be voted on the motion to defer, and that a written ballot would be required. Ballot forms were distributed, tellers were appointed, and the members voted. The tellers counted the ballots and reported that 372 members present voted for deferral and 326 against deferral, and that 75 proxies were voted in favor of deferral and 41 against deferral. The total vote was 447 for deferral and 367 against.

The failure of the meeting to approve the proposed amendment was reported in some detail in the financial press, sometimes with sarcasm, always without sympathy. The publicity was a source of humiliation to many members.

At the next annual meeting, in 1961, the same proposal was resubmitted. In the meantime there had been ample opportunity for discussion of the proposed rule at state society meetings and elsewhere. Articles and correspondence had been published on the subject.

An illegal motion to amend was ruled out of order, and a motion to table was defeated. Several speakers strongly opposed the proposed amendment; others strongly favored it.

The previous question was moved and seconded, and adopted by more than a two-thirds vote, thus cutting off further debate.

A written ballot was called for, tellers were appointed, and the balloting took place.

The tellers reported that 916 of those present voted in favor of the proposed amendment, and 130 against. Of the proxy votes cast, 2,021 were in favor and 191 against. The total was 2,937 in favor and 329 against.

In the subsequent vote of the entire membership by mail ballot, the proposed new Rule No. 13 was approved by more than two-thirds of those voting.

Its sponsors could be excused for a feeling of relief and satisfaction after their arduous campaign. But the adoption of the new rule by no means settled all the questions about auditors' independence.

Independence and Management Services

Even after the SEC had adopted its rules, it had taken the profession 28 more years to ban completely the most obvious relationships likely to raise doubts about the independence of auditors. But the debate about "relationships" which might mar the "appearance" of independence had barely begun.

The newly adopted Institute rule said, "A member or associate, before expressing his opinion on financial statements, has the responsibility of assessing his relationships with an enterprise to determine whether, in the circumstances, he might expect his opinion to be considered independent, objective and unbiased by one who had knowledge of all the facts."

This invited challenges to independence of a far more subtle and complex nature than those based solely on financial interest or joint service as auditor and officer or director.

For some years there had been expressions of concern about the extensions of CPA services into areas loosely described as "management services," "management advisory services," or

"management consulting." This concern arose partly because some of these services undertaken by some firms seemed unrelated to traditional accounting practice. But in some quarters the question was raised whether close association of the auditor with management, in the development of internal structure, procedures, and policies, might appear to outside observers to put him in a position involving potential conflicts of interest.

The first widely publicized discussion of this matter appeared in a monograph, *The Philosophy of Auditing,* by R. K. Mautz and Hussein A. Sharaf of the University of Illinois, published by the American Accounting Association in 1961—the year in which the Institute's new rule on independence was adopted. The authors, after an extensive analysis, came to the conclusion that management services—and, incidentally, tax services—tended to cloud the appearance of independence of the CPA in his capacity as auditor:

> There tends to come a time in any arrangement for management services when the mutuality of interest of the consultant and the client become so significant that the accountant ceases to be independent in the sense that we feel he should be for auditing purposes. . . . Does anyone really believe that we can offer the managerial consulting type of advice to management on a fee basis and still appear completely independent to alert and intelligent outsiders? More and more, independent auditors will work in the harsh, cold light of public scrutiny; it will not be enough that we feel we are independent and can convince our clients of the same fact. More and more we will have to convince others. . . .

The authors' recommendation was that the audit function be sharply separated from other types of services rendered by an accounting firm. This could be accomplished in larger firms by separation of audit staffs and audit partners from those engaged in other types of work. With respect to smaller firms, the authors concluded that since very few of them "make what may be called a public audit," they should be permitted to carry on as they were doing, performing a variety of services for their clients as "general practitioners."

To most practicing members of the profession, these conclu-

sions were totally unacceptable. They seemed highly theoretical, based on premises which were not in accord with the realities of practice, and an oversimplification of a complex subject.

However, this monograph was followed by articles by other professors expressing the same point of view. Discussion of the subject was not made any easier by the semantical difficulties involved in varying interpretations of the terms "management services," "advisory services," or "consulting services"—none of which had ever been authoritatively defined.

It was disturbing to practitioners to learn that highly respected members of the academic community had challenged the propriety of services of a kind which certified public accountants had been rendering for many decades—though not until more recently under such descriptions as "management services." Neither users of financial statements nor the business and financial community generally had expressed concern about the relation of such services to audit independence. Why these attacks from the academic community?

The Institute's committee on professional ethics concluded that some authoritative expression of opinion on this question was required for the guidance of the membership. Accordingly in 1963 the committee published its Opinion No. 12 on independence.

This opinion stated that normal professional or social relationships would not suggest a conflict of interest in the mind of a reasonable observer. The committee cited the 1947 statement of the Council of the Institute, asserting that independence is an attitude of mind, but recognized that to maintain public confidence it was imperative also to avoid relationships which might have the *appearance* of a conflict of interest. Opinion No. 12 continued:

> The committee does not intend to suggest, however, that the rendering of professional services other than the independent audit itself would suggest to a reasonable observer a conflict of interest. For example, in the areas of management advisory services and tax practice, so long as the CPA's services consist of advice and technical assistance, the committee can discern no likelihood of a conflict of

> interest arising from such services. It is a rare instance for management to surrender its responsibility to make management decisions. However, should a member make such decisions on matters affecting the company's financial position or results of operations, it would appear that his objectivity as independent auditor of the company's financial statements might well be impaired. Consequently such situations should be avoided.
>
> In summary, it is the opinion of the committee that there is no ethical reason why a member or associate may not properly perform professional services for clients in the areas of tax practice or management advisory services, and at the same time serve the same client as independent auditor, so long as he does not make management decisions or take positions which might impair that objectivity.

These assertions, however, did not satisfy all members of the academic accounting community. The *Accounting Review* for July 1965 contained an article by Arthur A. Schulte, Jr., then associate professor of accounting at the University of Portland, Oregon, entitled "Compatibility of Management Consulting and Auditing." The article stated that Opinion No. 12 offered no empirical evidence to support its contention that the rendering of management advisory services by a CPA to an enterprise of which he was also auditor would not suggest to a reasonable observer a conflict of interest.

Professor Schulte had conducted a mail survey of 504 financial executives of 131 of the largest financial institutions, and of 756 financial executives of 395 other financial institutions randomly selected. Two hundred eighty-two responses were obtained from the first group, and 383 from the second—in both cases a response in excess of 50 per cent.

Ninety-seven per cent of the respondents attached special importance to the CPA's audit independence. Forty-five per cent believed that management consulting did tend to impair audit independence, and 55 per cent believed that it did not. Analysis, however, indicated varying degrees of intensity of these opinions. In summary, 43 per cent of the respondents did not believe that management consulting seriously endangered the CPA's audit independence, 33 per cent believed

that it did, and 24 per cent were somewhat undecided.

Dr. Schulte concluded that the results should be a cause for serious concern on the part of the public accounting profession.

It was immediately noted by practitioners, however, that Dr. Schulte did not define the scope of "management consulting" as the term was used in his questionnaire. Nor did it contain any explanation of the CPA's role in performing such services. It was, therefore, impossible to determine exactly what the respondents to the questionnaire had in mind when they answered, or the extent to which they had given thoughtful consideration to the matter before answering. Were they indeed reasonable observers "who had knowledge of all the facts?"

Some of the questions in the questionnaire also seemed to be of a leading character, which tended to evoke responses which might not have occurred otherwise to those who answered the questions.

Pointing out these two alleged flaws in the survey, spokesmen for the Institute stated:

> It is difficult to believe that reasonable observers—stockholders, creditors or other users of financial statements, or the business public generally—would see any conflict of interest in the fact that the auditor, in addition to giving an opinion on the financial statements, also applied his technical knowledge and skill to the improvement of management's planning, control and decision-making processes.
>
> As a matter of fact, advice and assistance in improving clients' accounting systems and internal controls have been normal functions of auditors from time immemorial—functions which have never raised any questions about independence.
>
> Substantial benefits may result from combining the two functions. Knowledge of audit requirements can be useful in many types of management services, and the CPA must see to it that his recommendations meet the tests he would impose as auditor. Since management services are non-recurring, the audit fees are likely to be more important to the accounting firm in the long run. A poor management services job may risk the loss of the audit, but this tends to improve the quality of the consulting rather than impair the independence of the auditor.

Acknowledging that the line between advising and decision-making could not be drawn positively, the Institute's spokesmen continued:

> . . . It is possible to conceive of circumstances in which the auditor who performs management services might not be considered independent. The ethics committee has said that management rarely surrenders its responsibility to make management decisions, but if the auditor makes such decisions his objectivity might be impaired. The important point is that there is no basic incompatibility between the two functions. The auditor who also acts as consultant simply has one more factor to assess in determining whether a reasonable observer would regard him as subject to a conflict of interest.
>
> As in so many arguments, the absence of definition of terms causes semantic difficulties. "Management services" embraces a wide variety of activities, and the phrase means different things to different people. "Independence" is also susceptible to a variety of subjective interpretations.
>
> It is clear that a measure of confusion has been engendered within the profession on this important matter. It has arisen partly because of a tendency to extend to the ultimate theoretical limits the concept that the auditor must not only *be* but also *seem* independent. . . . But concern with appearances should not confuse appearance with reality. Too much emphasis on relationships which might conceivably suggest a conflict of interest to the most suspicious observer may be a disservice both to the profession and the public.
>
> The result might be to deprive clients of valuable creative contributions to improved management which their auditors, through their very familiarity with the clients' business, acquired in the course of the audit, are in a better position than anyone else to make. To split the accounting profession into two segments—one a group of ivory-tower auditors who did nothing but attest to the fairness of financial statements, and the other a group of experts in management and tax problems—would not only reverse the natural trend of accounting practice which has evolved over a century of experience; it would also add substantially to the cost of providing business with all the professional accounting service it needs. . . .
>
> To contend that a CPA acting as auditor should have no relations with his client except those involved in his work as auditor, for fear that the public might suspect a conflict of interest, would lead to an absurd situation. The auditor would be working in a vacuum. . . .

These statements on behalf of the Institute in turn evoked

critical reactions from Dr. Schulte and others. In July 1966, the *Accounting Review* published an article by Abraham J. Briloff, adjunct professor of accountancy at the Bernard M. Baruch School of Business and Public Administration, City College, New York, entitled "Old Myths and New Realities in Accountancy." This was only one of a series of articles dealing with independence by college professors which had appeared in various accounting publications in the preceding several years.

Professor Briloff's article, however, was notable for the fact that he also had sent a questionnaire to members of the financial community, as well as to members of the practicing and academic branches of the accounting profession. He found that 53 per cent of the respondents from the financial community felt that the rendering of management services by CPAs detracted from the significance of their opinions as independent auditors. In his article he pointed out that he had met objections voiced by Institute spokesmen: first, he had used the term "management services" instead of "management consulting"; second, he gave the respondents an opportunity to express their views regarding specific services offered by CPA firms as aids to management.

However, many of the specific services which he cited were those likely to appear to outside observers as unrelated to the accounting function, for example: "review all phases of the business in connection with a plan to extend profits"—only 28 per cent of the respondents from the financial community thought that this service should be rendered by CPAs; "prepare an executive development program"—only 3 per cent of the respondents from the financial community thought that this service should be rendered; "develop a plan of executive compensation (including 'fringe benefits')" —only 29 per cent of the respondents from the financial community believed that this service should be rendered; "determine market potentials and plan profitable sales territories"—only 3 per cent of the financial community believed that this service should be rendered; "analyze job functions

and responsibilities of the entity's personnel"—only 6 per cent of the respondents from the financial community believed that this service should be rendered.

There was no description of the precise role of the CPA in any of these service areas.

Professor Briloff asserted that his research "confirmed the existence of gaps between the understanding by the profession and the corresponding understanding by the financial community," and he referred to "the crisis in confidence, the crisis in integrity which presently confronts the profession."

At the annual meeting of the Institute at Boston in the fall of 1966, Manuel F. Cohen, chairman of the Securities and Exchange Commission, was one of the principal speakers. In the course of his remarks he showed that the debate about independence and management services had come to the attention of the Commission. He said:

> It is a truism, but no less significant, to note that the integrity and completeness of the required financial statements are the keystone around which is built the kind of investor confidence which supports our capital markets. In recognition of this grave responsibility, we have both expended considerable effort to define and implement this requirement of independence. It may, therefore, be appropriate for me to refer to the doubts now being raised in some quarters about the independence of the accountant who provides his audit clients with what is loosely called "management services."
>
> A recent book by Eric Kohler, an accountant well known to all of you, notes that "A public accountant's established services to management have also come to be of the first order of importance. These include the preparation of income-tax returns, or aid in their preparation or review; and forward planning on such diversified matters as budgetary procedures, costing methods, inventory controls, incentive plans, and pension schemes." These services may, in Mr. Kohler's words, be "natural consequences of the auditor's developed skills," and may "contribute to a better background for succeeding audits, as well as to better management." So long as they are directed toward those ends, they do not appear to pose a serious threat to the accountant's independent status.
>
> However, a word of caution is in order with respect to what one of your prominent members describes as "consulting services which

> cannot be related logically either to the financial process or to broadly defined information and control systems, [such as] market surveys, factory layout, psychological testing, or public opinion polls." And, I am disposed to add, executive recruitment for a fee. An accountant who directs or assists in programs of this kind raises serious questions concerning his independence when it comes time to render to creditors, to investors and to the public his opinion on the results of the programs. Public accountants should carefully reconsider their participation in these activities lest their continuation and extension undermine the main function of the independent accountant—auditing and the rendering of opinions on financial statements.

Mr. Cohen seemed to be saying that "management services" related to financial processes or to information and control systems raised no serious threat to independence. This was a distinction which Professors Mautz, Schulte, and Briloff had not made. Their findings seemed to condemn "management services," or "management consulting" as a field of activity, without regard to the nature of such services.

Tentative Conclusions

However, an official response from the Institute to all these criticisms seemed necessary.

Accordingly, a special ad hoc committee was established to study the problem, under the chairmanship of Malcolm M. Devore, a partner of Haskins & Sells, a former vice president of the Institute, and at the time of his appointment a member of the executive committee. With Mr. Devore were representatives of the committees on auditing procedure, ethics, management services, and taxation.

First, this committee read all the articles of which it had knowledge on the subject of management services in relation to audit independence. It corresponded with the authors of all these articles to seek their additional views on the subject. Messrs. Briloff and Schulte, who had based their criticisms on responses to questionnaires, were invited to meet with the

entire committee. Representatives of the committee also met with the chief accountant of the Securities and Exchange Commission to explore the matter further.

The committee then consulted representatives of groups whose members made use of audited financial statements, including the American Bankers Association, the Financial Analysts Federation, the Financial Executives Institute, and the Life Insurance Association of America. Officers of these organizations were asked to suggest the names of members who would be willing to talk with the committee on this subject. Most of the representatives of the four organizations were not personally acquainted with the members of the Institute committee. A full day was devoted to discussion with four or five representatives of each of these four groups.

At the 1967 annual meeting of the Institute an entire session was devoted to discussion of this problem. Dr. Schulte presented his point of view; a financial executive of a large insurance company, Mr. Frank Hoenemeyer, presented another point of view; and Mr. Devore summarized the findings of his committee to date. A summary of these talks was published in *The Journal of Accountancy.*

After further analysis and discussion, the committee submitted to the executive committee, in August 1968, an interim report which the executive committee authorized to be published and sent to a cross-section of members of the profession, including the academicians who had been most critical on the subject, and the 16 representatives of the financial community whom the committee had consulted. With only a few exceptions, the latter group approved the interim report. From the practicing members of the profession there was also general approval of the report, although the response was small. Of a total of 1,200 persons to whom copies were distributed only 70 replied. The academic members for the most part were not satisfied with the report but urged further research on the subject.

The report first recited the steps the committee had taken

to inform itself, and then submitted certain observations. First, it found a substantial misunderstanding as to the nature of management services rendered by CPAs and the manner in which such services were rendered. Second, the committee concluded that the subject was not susceptible to useful research by means of questionnaires. Lack of understanding on the part of recipients of the questionnaires as to the nature of the services discussed, and the role of the accountant in rendering them, posed one severe limitation on the value of questionnaires. Also, the difficulty of phrasing questions so as to elicit the desired information limited the usefulness of the questionnaire approach to such a complex subject.

The committee found no evidence that the rendition of management services had impaired the independence of CPAs *in fact,* but that some users of financial statements believed that such services created an *appearance* of lack of independence.

It was noted that the chairman of the SEC in his speech found nothing objectionable in management services related to the financial process or to broadly defined information and control systems, though he questioned such services as market surveys, factory layout, psychological testing, public-opinion polls, and executive recruiting.

The committee found difficulty in conceiving a sound rationale which would justify the proscription of these latter "so-called peripheral services," since it was not clear as to how each specific service might seem to impair the independence of an auditor. The committee noted that such services as psychological testing, public-opinion polls, and formal executive recruiting were rendered by relatively few firms, and represented only a minor part of their practice.

The committee recognized that services not related to the types of work which the public had become accustomed to associate with accountants in the past might seem strange and even inappropriate to some. However, this somewhat vague feeling on the part of a limited number of observers did not

seem to justify a proposal that this type of service be forbidden by amendment of the Code of Ethics.

The committee recommended exposure of two position papers prepared by the Institute's committee on management services—one, describing the nature of management services rendered by CPAs and their role in rendering such services; and the second, indicating standards of competence in these areas. It was hoped that these papers would clarify public understanding of what CPAs did in this area, and how they did it.

The committee also stressed the importance of having CPAs avoid a decision-making role in their management advisory work, and emphasized the necessity of strict observance of the Code of Ethics in management services as well as in other areas of practice.

The committee endorsed a proposal of the Institute's executive committee that corporations create audit committees composed of outside directors, which would recommend the appointment of auditors, and discuss with them any problems arising in the course of their engagement. The special committee suggested that if a CPA had any question about the propriety of a particular service to management of a company of which he was also independent auditor, he might discuss the problem with the audit committee, or with the full board of directors, to make sure that the stockholders' representatives concurred in the decision.

In view of the apparent lack of interest generated by the exposure of this tentative report, the Devore committee suggested to the executive committee that it may have overreacted to the criticisms of the several preceding years. While no definitive answers to the critics could be given at the present time, it was suggested that continual attention be given to the questions that had been raised.

Fundamentally, it appeared that this type of problem would have to be solved on a case-by-case basis—a common-law approach rather than a statutory approach—since the

circumstances in each case might have a bearing on the question whether the appearance of independence would be likely to be impaired or not.

In the 30-odd years between 1936 and the late sixties, tremendous strides were made in clarifying the essential concepts of audit responsibility. Standards were set up, acceptable procedures were described, and the elusive concept of independence was carefully re-examined. As these things were done, the prestige of independent auditors rose steadily—the public began to pay more attention to their reports and to place heavier reliance on them.

As a natural result, the accounting profession became a more visible target for criticism and challenge. The willingness of the American Institute of Certified Public Accountants to re-examine its own assumptions as to the profession's proper role in society, its standards, its procedures, and its traditional ways of doing things was an essential contribution to progress.

While progress in democratic institutions requires consultation on a broad scale before final decisions can be reached, and therefore often seems slow, in retrospect the progress in evolving audit responsibility over a mere few decades was impressive. The acceptance of greater responsibility, while it has its risks, is clearly the price of increasing public confidence and broadening opportunities for service.

CHAPTER 9

The Defense of Tax Practice

IN THE early 1930's only a small proportion of the nation's citizens had enough income to require payment of individual income taxes—despite the fact that the income-tax law had been in existence for two decades. Business enterprises, however, generally had income taxes to pay. Inasmuch as the calculation of business income required accounting knowledge, businessmen turned to CPAs in large numbers for help in preparing their returns, and in dealings with the Bureau of Internal Revenue. Tax practice had become a large part of the total volume of professional accounting service.

Tax practice was an unfamiliar field for most lawyers, and for a long time few of them paid much attention to taxes. Indeed, many lawyers had their own tax returns prepared by accountants.

However, as tax disputes increased, and more cases were taken to the Board of Tax Appeals and the courts, lawyers began to be drawn into tax practice, and some of them began to specialize in it.

As noted in Volume I of this work, the bar associations in the early thirties made the first disturbing suggestions that the tax practice of CPAs was in part, at least, an illegal invasion of the field reserved for lawyers.

The first alarm was an unsuccessful effort in 1932 to eliminate CPAs from practice before the Board of Tax Appeals.

The second alarm was a bill introduced in Congress, which would have limited the rights of non-lawyers to represent others before federal agencies. This was also defeated.

However, similar efforts began to be made in the states, by local bar associations, to limit to attorneys appearances before state commissions and boards; and to confine to attorneys the preparation of papers or documents related to proceedings before such bodies.

Discussions between leaders of the two professions seemed desirable. Early meetings between representatives of the Institute and the American Bar Association resulted in nothing but a polite exchange of views. However, the Institute created a committee on co-operation with the Bar Association to give continuing consideration to what seemed a growing problem.

In 1936 a New York court held that a non-certified accountant had practiced law in giving advice on possible recovery of state income taxes, and therefore could not recover his fee.

The American Bar Association was actively supporting bills in Congress governing the procedure of administrative agencies. Some of these bills contained ambiguous language regarding representation before such agencies, which could have been construed so as to limit the ability of CPAs to practice before the Board of Tax Appeals and the Treasury Department.

The National Organizations Disagree

In 1936 the American Bar Association's committee on unauthorized practice of the law charged, in general terms, that accountants were invading the practice of law by legal work which they were not authorized to do. The Institute committee was asked whether it could control the members of their profession, as did the American Bar Association. If not, the lawyers indicated that they would have to obtain injunctive relief, if not legislation, in order to correct the situation. The Institute committee responded that the accounting profession certainly could stop any improper practices by its members, but that it was necessary to have specific complaints before effective action could be taken. It was agreed that closer co-operation between the committees of the two associations would be desirable.

Later, two members of the Bar Association's unauthorized practice committee sent a questionnaire to corresponding local bar committees inviting specific information about activities of accountants which might be regarded as unauthorized practice of law.

One month after the issuance of this letter, a joint meeting of the Institute and Bar Association committees occurred in Washington. The Bar committee's chairman suggested that if the two organizations could agree on broad principles covering the proper scope of activity of the two professions, a statement might be released jointly for the information of both accountants and lawyers. The Institute's committee thought this would be desirable.

There followed a discussion of specific questions. The first was whether accountants should organize corporations, prepare articles of incorporation, charters, bylaws, and minutes of organization meetings. Institute spokesmen agreed without hesitation that accountants should neither do these things nor prepare papers necessary for corporate reorganizations, such as resolutions.

Both groups agreed that neither accountants nor lawyers

should solicit tax claims, and that accountants and lawyers should not split fees on work which they did jointly.

A more difficult question was to what extent accountants should give advice and opinions on taxation. The lawyers suggested that advice on how to save taxes, or on matters involved in tax controversies, would require interpretation of statutes and court decisions, which they regarded as the practice of law. After discussion, there was general agreement that it was necessary for both an accountant and an attorney to be consulted in important cases of these kinds.

Practice before the Board of Tax Appeals was discussed. The Institute representatives acknowledged that it was unwise for an accountant to attempt to argue a case before the Board without the advice of an attorney, since, for one thing, the rules of evidence applied; but they would not concede that accountants should be limited to the role of expert witnesses. The lawyers expressed the view that in appearances before boards and commissions CPAs should confine themselves to the presentation of accounting data and should not argue legal points.

The Bar Association committee undertook to draft a memorandum covering these points, to be submitted to the Institute for review, with the objective of joint publication for the information of both professions.

The draft of such a memorandum received by the Institute committee stated a number of specific limitations on the activities of accountants, including the following:

> 8. It is generally not prudent nor in the client's interest for an accountant to prepare and present a contested tax case before the U.S. Board of Tax Appeals or any like administrative tribunal.
>
> 9. The division of responsibility between lawyers and accountants in dealing with the tax problems of a client should be determined in accordance with the following general rules: the accountant is indispensable in making mathematical computations, in making audit reports, in analyzing, scheduling, abstracting and marshalling the contents of financial records and the results of financial transactions. Questions involving the validity of statutory enactments, or regulations, or the interpretation thereof, or the effect of a settlement

agreement should not be answered by an accountant but should be a subject for legal advice. Inasmuch as the rights of taxpayers are fixed by the contents of protests or claims for refund, every such statement should be prepared by a lawyer. Discussions with governmental authorities with respect to accounting questions may properly be conducted on behalf of taxpayers by accountants, but the presentation of proofs and arguments belongs to the field of the lawyer.

The Institute's committee took exception to the tone of this memorandum and, in particular, to item 9. The Bar committee explained that the memorandum was submitted simply as a basis for discussion—generally summarizing the lawyers' understanding of the conclusions reached at the preceding meeting.

The chairman of the Institute's committee was Francis P. Byerly, a partner of Price Waterhouse & Co. and a man of superior intellect, pleasant personality, and calm self-confidence.

Mr. Byerly expressed the view that it would be futile to attempt to draw sharp lines dividing the activities of lawyers and accountants in tax practice, which necessarily often overlapped. He objected to the one-sided manner in which some of the points in the memorandum were stated. With specific reference to items 8 and 9, he said that there would be difficulties of application in practice—that accountants and lawyers should co-operate in many cases, but that it could not be conceded that the preparation of papers to be filed by taxpayers in all cases was the exclusive field of the lawyer.

It was agreed that both groups should attempt to revise the memorandum in line with this exchange of views.

One month later the Institute's committee sent to the chairman of the Bar committee a revised draft, emphasizing that the two professions were often required to work together in the best interest of the client; and that it was impracticable to formulate mutually exclusive definitions of the practice of law and accounting. The draft stated that exclusively within the field of law were the trial of cases, the drawing of documents, such as deeds, wills, trust agreements, contracts, etc.,

and that exclusively within the field of accounting were the examination of books of account and business records and operations, and expressions of opinion on financial statements. Tax work was said to be a field where the two professions overlap. The importance of accounting in the determination of taxable income was emphasized. When a tax dispute was carried to the court, it was stated, the case must be handled by an attorney; however, there were many areas which either CPAs or attorneys were qualified to handle, and rigid rules could not be laid down defining the role of each in all cases.

In April 1938 the Institute received from the Bar committee a revised draft of a statement of principles, which prominently alluded to a provision of Treasury Department Circular 230 to the effect that nothing contained therein authorized the practice of law by enrolled agents who were not lawyers. The draft stated that professional advice regarding legal rights and remedies, or involving the application of rules of law to factual problems, constituted the practice of law. It also alleged that professional representation of other persons before courts, administrative offices, or agencies of government, in the assertion of legal rights and remedies, constituted the practice of law. Further, it was stated that whenever, in connection with the defense or assertion of a taxpayer's rights, there arose questions, whether on the substance of law or procedure, the solution of which required the professional knowledge and skill of a lawyer, the decision could not properly be made by laymen.

In conclusion, the draft stated, the committee on unauthorized practice believed that all the following activities constituted the practice of law: the conduct of trials before the Board of Tax Appeals; the drafting of petitions, stipulations, or orders incident to review of assessments by the U.S. Board of Tax Appeals; the drafting of protests against tax adjustments, deficiencies, or assessments; the drafting of claims for refund; the giving of advice regarding the validity of tax statutes or regulations, or advice regarding the effect thereof in respect of matters outside of accounting procedure; and the representa-

tion of taxpayers at conferences with administrative authorities in relation to matters outside of accounting procedure.

The memorandum stated that these conclusions were not concurred in by the Institute committee. The positions of the two committees were obviously far apart.

The Bar committee indicated an intention to publish in its annual report a statement similar to the draft submitted to the Institute's committee.

Mr. Byerly objected to premature publication of the statement without an opportunity for further discussion before the Bar committee assumed a unilateral position on this important question.

Nevertheless, the report of the Bar Association's unauthorized practice committee was published. It contained the following statement:

> It is the view of the committee that it is the practice of the law to engage in any of the following activities: (1) to give advice regarding the validity of tax statutes or regulations or the effect thereof in respect of matters outside of accounting procedure; (2) to determine legal questions, preliminary or prerequisite to the making of lawful returns in a lawful manner; (3) to prepare protests against tax adjustments, deficiencies or assessments; (4) to represent a taxpayer at a conference with administrative authorities in relation to matters outside of accounting procedures; (5) to prepare claims for refund of taxes; (6) to prepare petitions, stipulations or orders incident to the review of assessments by the U.S. Board of Tax Appeals or any like administrative tribunal; (7) to conduct a trial of issues before the U.S. Board of Tax Appeals or any like administrative tribunal.

A meeting of the two committees was held at Cleveland on July 25, 1938, in another effort to resolve their differences.

Mr. Byerly took a strong position. He said that the Institute committee disagreed completely with portions of the Bar committee's report and that, since that report had been published, the Institute's committee must publish its own views on the matter for the information of the accounting profession. He expressed regret that a joint statement acceptable to both

groups could not be published, instead of statements of conflicting views.

The chairman of the Bar committee assured the accountants that the Bar was not aiming at action against members of the Institute or, for the most part, against CPAs, but that many complaints had been received of improper practices by accountants who were not certified. His committee's report, he said, had intended only to block out the general areas of the subject matter for careful consideration; that the American Bar Association would not be requested to approve or endorse the report; and that the report could be altered if his committee was convinced that this was desirable.

Mr. Byerly pointed out that the publicity the report had received might well encourage local bar associations to seek injunctions against CPAs and members of the Institute, as well as others.

He then suggested that the problem could best be dealt with on the basis of complaints in specific cases, rather than by broad statements of principle. He assured the Bar representatives that the state societies and the Institute would be glad to investigate any complaints of improper practices by accountants, certified or non-certified.

The Bar committee received this suggestion favorably.

The accountants then asked whether the Bar committee would modify the conclusions in its published report, and the lawyers agreed to give consideration to this possibility.

After discussion of specific points in the Bar committee's report—the accountants pointing out that interpretation would be very difficult in the absence of definitions of "accounting procedure" and "legal questions"—the meeting adjourned in order to give the Bar committee an opportunity to reconsider its position.

In the meantime the Institute committee decided to prepare a letter to the Board of Governors of the Bar Association objecting to the unauthorized practice committee's report. This letter was drafted.

When the two committees reconvened, the lawyers pre-

sented a statement to the effect that the present report of the Bar committee was subject to re-examination and clarification, and that co-operation between the two committees would be continued. Mr. Byerly then described the contents of his committee's letter to the Board of Governors of the Bar Association.

After the Institute's letter had been presented to the Board of Governors, publication of the whole story was authorized on both sides. Mr. Byerly prepared an article entitled, "Relationship Between the Practice of Law and Accounting," published in *The Journal of Accountancy* for September 1938, in which it was stated that the Institute committee could not agree with the Bar committee's report; that the Bar committee had indicated that its conclusions were necessarily general in character; that it had been agreed to investigate complaints in specific cases, and that co-operative activities would be continued, including a re-examination and clarification of the conclusions expressed in the report.

The 1939 annual report of the American Bar committee reported the Cleveland meeting with the Institute's committee, stating that no agreement had been reached on a general statement of principles, but that co-operation in investigating complaints had been arranged. Meanwhile, local bar organizations were encouraged to confer with representatives of the state societies of certified public accountants on the same issues.

Thus matters rested. No meetings of the national committees took place during the next four years. The action shifted to Washington and to the states.

Representation of Taxpayers

In the spring of 1939 Institute representatives met informally with members of the United States Board of Tax Appeals, some of whom had complained about the manner in which some CPAs had presented clients' cases before the

Board without associating themselves with attorneys. As a result, the Institute advised state societies that while there was no immediate disposition on the part of the Board to exclude CPAs from practice before it, it would be advantageous if CPAs were discouraged from trying cases before the Board without the assistance of attorneys. In the July 1939 *Journal of Accountancy* an editorial repeated this advice.

In 1941 a hearing took place before the Senate Judiciary Committee on a bill to revise the administrative procedure of federal agencies. C. Oliver Wellington, later to become a president of the Institute, represented the accounting profession. This bill contained a provision designed to "regularize the circumstances in which others than members of the bar may properly appear before such agencies." Mr. Wellington pointed out the existing rights of certified public accountants to appear before certain agencies, particularly the Treasury Department, and argued that in the public interest these rights should not be curtailed. Senator O'Mahoney, acting as chairman of the committee, assured Mr. Wellington that there was no intention of altering the status of CPAs in their tax practice and said that there need be no concern about the possibility of any change in that direction.

The 1942 Revenue Act provided that the name of the Board of Tax Appeals should be changed to the "United States Tax Court." The House Ways and Means Committee insisted on assurance that no matter what the name of the organization, it would remain an administrative tribunal rather than become a part of the judiciary. Representative Dingell of Michigan, perhaps at the insistence of an accountant constituent, introduced an amendment which was adopted, providing that practice before the Court could not be denied to any person because of his failure to be a member of any particular profession or calling. The Institute's tax committee opposed this provision, recognizing that while it might appear to protect the rights of CPAs, it might, in fact, be detrimental in admitting to practice before the Court others than lawyers and certified public accountants, who from the beginning had been given equal

status and the exclusive privilege of practice before the Board of Tax Appeals.

However, the bill passed with the Dingell amendment. The Tax Court then announced, in effect, that since it could not bar anyone from practice before it because of his failure to be a member of any particular profession or calling, it would have to set examinations for admission to practice. Lawyers were exempted from this examination, on the presumption that they were familiar with the rules of evidence and the procedures followed by the Court. CPAs, however, were required to pass the examination. Efforts by the Institute to have the Court restore the right of CPAs to admission without examination were unsuccessful.

As a practical matter, CPAs seemed to be fighting a lost cause in their efforts to maintain an equal position with lawyers in this particular forum—a position in which the accounting profession had taken great pride.

In 1943, five bills were introduced in Congress dealing with procedure of federal agencies, all of which contained some reference to practice before such agencies, and a few of which were clearly adverse to CPAs. The Institute registered its opposition to these bills, and was prepared to testify at hearings, but Congress took no action.

Local Action

During 1942 and 1943, the American Bar Association's unauthorized practice committee was comparatively inactive—partly, no doubt, because of wartime conditions.

Local bar associations, however, were putting increased pressure on the CPAs.

During the decade in which the controversy had been developing, the Institute received reports of pressures on state societies in 14 states, which in order of occurrence were as follows: New York, Virigina, Louisiana, Minnesota, Missouri,

Ohio, Illinois, Pennsylvania, Wisconsin, Arkansas, Colorado, Connecticut, Rhode Island, and Massachusetts.

These pressures took various forms. In some cases efforts were made to persuade CPAs to sign voluntary agreements which would have limited the scope of their practice. On the advice of the Institute that federal tax practice should be dealt with at the national level, most of the state societies refused to join in such agreements. Some bar associations introduced bills in state legislatures which would have limited customary activities of CPAs. The CPAs often opposed such bills successfully. In other instances local tax commissions or boards were persuaded to alter their regulations so as to limit the scope of accountants' practice before them.

The greatest danger, however, as it soon became clear, was through action in the state and local courts. Accountants who sued for fees for tax services began to find that they were opposed with the contention that they had engaged in the unauthorized practice of law. The courts had the power to regulate the practice of law, and therefore to determine what it was.

The local bar associations, accordingly, could apply to the courts for injunctive relief. In 1943, the Lowell, Massachusetts Bar Association sought an injunction against a noncertified accountant named Loeb and associates who had advertised their readiness to make out tax returns for a fee. In the lower court an injunction was granted, forbidding them from continuing to prepare tax returns, on the ground that this was the practice of law.

The case was appealed to the Supreme Court of Massachusetts. The Massachusetts Society of Certified Public Accountants filed a brief as a friend of the court, protesting the trial court's decision. The Supreme Court reversed that decision, stating that the preparation of simple tax returns for individuals, with which the Loeb organization was mainly concerned, was not the practice of law. The Court, however, specifically left open the question whether the preparation of complex tax returns might constitute the practice of law.

Formation of National Conference

Under date of January 5, 1944, David F. Maxwell, the new chairman of the American Bar Association's committee on the unauthorized practice of law, wrote to Victor H. Stempf, then president of the Institute. The letter referred to complaints from all parts of the country that unscrupulous and untrained persons were preparing income-tax returns to the detriment of the public, and expressed the hope that present evils might be eliminated by co-operative efforts of the Bar Association and the Institute. Mr. Maxwell invited the Institute to send a representative to the next meeting of his committee, to be held in St. Louis, for the purpose of considering means of eliminating such "unlawful activities."

William Charles of St. Louis had succeeded Mr. Byerly as chairman of the Institute's committee on co-operation with bar associations. He attended the meeting of Mr. Maxwell's committee and reminded the lawyers present of the numerous discussions between representatives of the two organizations in the past. Mr. Charles also suggested that the Bar establish a committee on co-operation with accountants, instead of dealing with the Institute solely through its "unauthorized practice" committee.

Mr. Maxwell said that the Bar Association had formed "conferences" with other groups, such as bankers and real-estate brokers, to consider in a co-operative manner problems of mutual interest. He proposed that the American Institute and the American Bar Association form a National Conference of Lawyers and Certified Public Accountants. This idea appealed to Mr. Charles and his committee. The governing bodies of the two national organizations also approved, and the National Conference of Lawyers and Certified Public Accountants was established a few months later. Representatives of the Bar Association included a member of its board of governors, the vice-chairman of its tax section, a representative of the administrative law committee, and two members of the unauthorized practice committee. The Institute's representatives included the

chairman of the committee on co-operation with the Bar Association, a past president and member of the ethics committee, the chairman of the tax committee, a member of the executive committee, and the chairman of the committee on co-operation with the SEC.

A joint release to the press announcing formation of the Conference indicated that controversial questions would be minimized. The presidents of the Institute and the Bar Association were quoted as saying that, in modern times, more and more the average citizen was required to seek the professional services of both accountants and lawyers; harm and injury resulted when such services were rendered by unqualified persons; the American Bar Association and the American Institute had been created to aid their members and serve the public; they had continually raised their standards of practice, enforced codes of ethics and insisted on higher qualifications; and that one of the objectives of the National Conference would be to co-ordinate the common efforts of these two great associations to improve and expand the usefulness to the public of both.

In an atmosphere of cordiality evoked by these sentiments, the first working meeting of the Conference was held at Philadelphia, May 6, 1944. A statement of objectives consistent with the press release was adopted. Subcommittees were appointed to study various problems and report back. One of the subcommittees was assigned the objective of considering misunderstandings involving fundamental issues between the two professions and recommending means for disposing of them. The next meeting of the Conference was set for September 10, 1944, in Chicago.

A Dash of Cold Water

The Institute members were encouraged by the friendly and reasonable attitude of the lawyers at the first Conference meeting. But their optimism was cooled when they received a copy of the report of the American Bar Association's unauthorized prac-

tice committee, prior to the annual meeting of the Association in August—one month before the coming Conference meeting. David Maxwell, who was co-chairman of the National Conference, was also chairman of the unauthorized practice committee. The report of this committee referred to the Conference, expressing the hope that it could agree on where the practice of accountancy ended and the practice of law began. But the report went on to say that since the Revenue Act of 1944 had simplified income-tax returns for the average individual, there was no further necessity for distinction between simple and complicated income-tax returns. Preparation of all income-tax returns, other than the optional ones for individuals with income less than $5,000, should be construed as the practice of law, the report declared. Hence local committees were advised to act promptly to prevent unqualified individuals from preparing such returns. Reference was made to the Massachusetts Supreme Court decision in the *Loeb* case, leaving open the question whether preparation of complicated tax returns was the practice of law. The report said, "However, in the opinion of your committee this case may be used as authority in any suit to prevent an unqualified person from preparing a more complicated tax return under the new revenue law."

At the September meeting of the Conference the Institute's representatives objected strongly and bluntly to the statements in the report of the unauthorized practice committee, pointing out that there was no reason why local bar associations would not accept these statements as applying to CPAs as well as others. Mr. Maxwell protested that this was not intended—that by "unqualified individuals" his committee meant the so-called "fly-by-nights."

The lawyers were conciliatory. It was suggested that Mr. Maxwell appear before the House of Delegates, and make a statement for the record that the pertinent passages of his committee's report did not apply to certified public accountants.

After further discussion, the Conference adopted a resolution to the effect that the public would be best served if income-tax returns were prepared either by certified public account-

ants or lawyers; that it was in the public interest for members of each profession to recommend the employment of members of the other in appropriate circumstances; and that CPAs should not prepare legal documents such as articles of incorporation, bylaws, contracts, deeds, trust agreements, wills, and similar documents.

Subsequently, Mr. Maxwell appeared before the House of Delegates and made a statement that the recommendation in his committee's report was not pointed at certified public accountants, whom the committee recognized as professional men, qualified by education and training to prepare income-tax returns. Rather, he said, the report was directed against the thousands of unqualified persons engaging in this activity.

The Bercu *Case*

In April 1945 the Institute learned that Bernard Bercu, a CPA and a member of the New York State Society, had sued a client for a fee for services consisting of tax advice. The case was dismissed by the court on plea of the defendant's counsel that Bercu was practicing law without a license. It was understood that Bercu intended to appeal, and it was rumored that the New York County Lawyers Association would enter the case as friend of the court. All members of the National Conference of Lawyers and Certified Public Accountants were notified of this decision.

At the next meeting of the Conference it was announced that Bercu would withdraw his appeal. In the circumstances, it was the sense of the Conference members that no action was necessary.

However, it was subsequently learned that the New York County Lawyers Association was bringing injunction and contempt proceedings against Bernard Bercu for having engaged in illegal practice of the law by rendering tax advice for a fee.

Edwin Otterbourg was chairman of the New York County

Lawyers Association's committee on unauthorized practice of law. He was also a member of the National Conference, and co-chairman of a newly formed New York Conference of Lawyers and Certified Public Accountants, organized by the New York State Society of Certified Public Accountants and the New York State Bar Association. The issues involved in the *Bercu* case were never discussed on the merits either in the National Conference or the New York State Conference.

The New York society undertook to help Bercu defend himself in the injunction and contempt proceedings. The Institute agreed to assist the state society in defraying the costs involved. The state society engaged as counsel Mathias F. Correa, a member of a prominent New York law firm, and a lawyer of superior intellect and long experience in trial work. In 1947 the case was tried. The trial court handed down a decision favorable to Bercu, holding that he did not engage in the unauthorized practice of law in rendering the services to which the County Lawyers Association had objected.

The Association appealed this decision. In April 1948 an intermediate appellate court reversed the trial court's decision and held Bercu guilty of unauthorized practice of law in giving tax advice to a taxpayer who was not a regular client of Bercu. The appellate court drew a distinction between giving an opinion on tax matters to one for whom the accountant had not made up the tax return, or performed any auditing or accounting service, and a case in which such tax advice was incidental to regular accounting services.

The New York State Society decided to carry the case to the highest court in New York State, the New York Court of Appeals, and the Institute promised continued backing.

Hearings were held before the Court of Appeals, but in the spring of 1949 the court sustained without opinion the decision of the intermediate appellate court. Thus it appeared that in New York it would be illegal for a CPA to give tax advice to a client whose income-tax returns he had not prepared or for whom he had not rendered any other accounting services.

While the *Bercu* case was being fought, relations between the

Institute and the American Bar Association became steadily worse.

The CPA members resented the fact that some unauthorized practice committees of local bar associations were attempting to solve the problem by force—by resort to the courts—without adequate consideration of the complexities of tax practice, and the close interrelationship of law and accounting which it involved.

It was feared that the national and state Conferences of Lawyers and CPAs might be used to keep the accounting profession busy talking, while the unauthorized practice committees brought specific cases before the courts in order to build up common-law precedents limiting the scope of the CPAs' tax practice.

The Drift Toward Conflict

In 1946 and 1947 efforts to arrange a meeting of the National Conference of Lawyers and CPAs at a time and place satisfactory to both groups were unsuccessful.

Meanwhile, several state bar associations issued statements on tax practice which were regarded as hostile to the accounting profession.

Further, representatives of the American Bar Association sponsored in Congress an Administrative Practitioners Bill, which provided for enrollment of all practitioners before administrative agencies of the federal government. Lawyers would be accepted for enrollment on a showing of their professional status. Others would have to conform with certain provisions of the bill which could have created great difficulties for CPAs. After careful study the Institute decided to oppose the bill and to appear at hearings against it.

Shortly afterward another bill was introduced containing a provision to make the Tax Court a court of record. At the Institute's request, this bill was amended to provide that no

person should be barred from practice before the Tax Court because of his failure to be a member of any particular profession or calling—a provision identical with that of the 1942 Revenue Act providing for the change of name from Board of Tax Appeals to Tax Court. Bar association spokesmen attacked the Institute's amendment on the ground that it would be an affront to the dignity of a court to be forced to admit laymen to practice before it.

In 1947, John D. Randall became chairman of the American Bar Association committee on unauthorized practice of law, and co-chairman of the National Conference of Lawyers and CPAs, succeeding Mr. Maxwell. Mr. Randall testified in favor of the Administrative Practitioners Bill before the House Judiciary Committee in July 1947, and what he said contained no comfort for the accounting profession.

In 1948 hearings were held on both the bill to make the Tax Court a court of record and the Administrative Practitioners Bill. Testimony was presented by representatives of bar associations and representatives of the Institute and several state societies. The views of the two groups were in direct and sometimes sharp conflict.

The proposed change in status of the Tax Court was dropped, leaving that body as before, an agency in the executive branch of the government.

The Administrative Practitioners Bill was completely redrafted so as to eliminate many points to which the Institute had objected. Congress adjourned without taking any action on this bill.

The Bar's reaction to the Institute's testimony was acrimonious. *The Unauthorized Practice News,* a bulletin published by the American Bar's unauthorized practice committee, described the Institute's brief as "a masterpiece of innuendo, specious pleas, irrelevancies, and evasions of the essential issue," and said that it did not "hesitate to belittle the legal profession."

At this point the Institute prepared a statement of its position on the controversial questions involved in tax practice,

and published it in *The Journal of Accountancy* for March 1948. State societies were asked to encourage their members to convey this point of view to clients and others interested.

The statement emphasized the difficulty of drawing a clear line between the functions of lawyers and accountants in tax practice. The important role of accountants in tax matters over a period of nearly 40 years was stressed. The first requirement for the preparation of an income-tax return, the statement said, was the determination of income—basically a problem of accounting. It was recognized that the services of lawyers were necessary when legal problems arose and that accountants should not attempt to settle questions such as domicile, the laws applicable to trust funds, or the construction of wills.

Co-operation between the two professions, rather than conflict, was called for in the interest of the public as a whole.

The Conway *Case*

In 1948 the unauthorized practice committee of the Ramsey County Bar Association, Minnesota, brought suit for an injunction against a non-certified tax practitioner named Conway, on the ground that he had engaged in the unauthorized practice of law in offering advice to a supposed taxpayer whose return Conway had been asked to prepare. Actually, the supposed taxpayer was an agent of the bar association—it was a clear case of entrapment. Some of the carefully framed questions which Conway had been asked to answer involved alleged "legal" questions, including whether certain money spent on improvement of a building was deductible from earnings, and whether produce loss sustained by frost and flood was a deductible item.

The Minnesota Society of Certified Public Accountants decided to enter the case in an effort to prevent a sweeping de-

cision unfavorable to CPAs. Institute representatives conferred with Minnesota society officers and legal counsel, and offered the co-operation of the national organization.

Mounting Concern

The Institute's Council in its 1948 report to the membership made it clear that developments were viewed with grave concern. The report stated:

> The Institute was largely responsible for preventing passage of two bills in Congress which would have restricted the activities of non-lawyers to practice before federal agencies and before the Tax Court. . . . It is already practically certain that bills to accomplish the same purposes will be reintroduced. . . .
>
> The decision of the [trial court] in the *Bercu* case, holding in general that a certified public accountant might properly give tax advice to persons other than his regular clients, was reversed in the Appellate Division. . . .
>
> The Institute has offered its co-operation to the Minnesota Society of Certified Public Accountants in its effort to prevent a decision unfavorable to the accounting profession in the *Conway* case. . . .

Reference was also made to activities at the state level. The Council's report continued:

> All these matters have introduced uncertainty and confusion in the field of tax practice. The National Conference of Lawyers and Certified Public Accountants has been wholly inactive for the simple reason that there could be no hope of settling issues around the conference table which had already been publicly thrown into controversy before the courts and the Congress. Representatives of the Institute have conferred with representatives of the Treasury Department to consider the extent to which it may be possible for the Treasury to take the lead in bringing order out of what threatens to become a chaotic condition in the field of tax practice. Conferences with the Treasury and representatives of the American Bar Association are expected to occur in the coming months.

Appeals to the Federal Government

In the fall of 1948, the Institute approached the Treasury Department with a suggestion that consideration be given to the possibility of regulating practitioners who prepared tax returns, in somewhat the same manner as agents representing taxpayers before the Treasury Department were regulated. The Institute reasoned that preparation of federal tax returns, being an integral part of the collection of the federal revenues, should not be subject to the jurisdiction of state and local courts—as in the *Bercu* and *Conway* cases—whose decisions inevitably would vary widely with variations in the factual issues presented. The recent trend of events might lead to complete confusion as to who could do what in the federal tax field.

A conference was arranged in Washington in November, attended by representatives of the Institute, the tax section of the American Bar Association, the Treasury Department committee on practice, and the Bureau of Internal Revenue. After a full morning of discussion it was the conclusion of the government representatives that it would be impracticable to register, discipline, or attempt to control the estimated 300,000 persons who prepared tax returns for others. It was said that most of these persons knew more about simple tax returns than the average taxpayer did, and were therefore helpful to the Bureau in collecting the nation's revenues. It was clear that the Bureau did not favor limitation of the preparation of tax returns to lawyers or certified public accountants or both.

Thereafter, representatives of the Institute informally approached members of the American Bar Association's tax section, suggesting that relations between the two professions might be improved if the Bar were represented by lawyers most familiar with tax practice. This suggestion received a sympathetic reception. The House of Delegates of the American Bar Association adopted a resolution, which in effect instructed the unauthorized practice committee to consult with the tax

section on matters involving tax practice and relations with certified public accountants in that field.

Another Blow

Without warning, under date of December 10, 1948, Mr. Randall, as chairman of the national unauthorized practice committee, sent a circular letter to all members of the House of Delegates of the American Bar Association, and to the presidents and secretaries of all state and local bar associations. This letter stated that his committee refused to compromise certain principles relating to the "practice of law" by CPAs in the "tax law field," and made the following declarations:

1. A CPA was not qualified to advise a taxpayer as to his election of legal remedies—the Tax Court, a District Court, or the Court of Claims—when a wrongful assessment was to be contested.
2. A petition to the Tax Court was a legal document, and an accountant who drew it was engaged in the practice of law.
3. A claim for refund might provide the basis for litigation, and when an accountant prepared such a claim he engaged in the practice of law.
4. The fact that CPAs were admitted to practice before the Treasury Department did not authorize them to practice law or to give legal opinions, and, in the opinion of the unauthorized practice committee, the time had come, in the public interest, to review the general rules of practice before the Treasury Department.
5. Publicity put out by accountants had led the public and some lawyers to believe that tax law involved only accounting concepts.
6. The accountants' societies had opposed the change of the Tax Court to a court of record and had opposed the

Administrative Practitioners Bill, which had been supported by the unauthorized practice committee.

7. The committee believed that accountants were assuming the function of lawyers in the areas described, and the legal profession would not support any compromise or concession on the basic principles involved.

Mr. Randall was advised informally that the accounting profession disagreed with much of his letter, and that none of these issues had been referred to the National Conference of Lawyers and Certified Public Accountants for discussion. The question was raised whether the National Conference could accomplish anything useful if unilateral statements were to be made on both sides.

The president of the Institute, then Percival F. Brundage, also wrote to the president of the American Bar Association to protest Mr. Randall's action. The distribution of his letter to members of the Bar's House of Delegates and to officers of local bar associations, Mr. Brundage said, would stir up antagonism between the two professions, and create the false impression that CPAs generally were practicing law. Mr. Brundage asked the president of the Bar Association to take steps to avoid such unilateral pronouncements and to make arrangements through which the issues could be discussed in good faith by representatives of the interested groups.

The president of the Bar Association replied that the American Bar and its members were anxious to work in co-operation with the Institute, and that he would take the matter up with Mr. Randall.

There followed an informal exchange of correspondence and a personal discussion with Mr. Randall, as a result of which he expressed willingness to meet informally with Institute representatives and representatives of the tax section of the American Bar Association, to discuss all items in controversy and to consider the possibility of restoring the National Conference. This meeting was arranged for March 15, 1949, in Washington.

More Action on the Legislative Front

Meanwhile, a new version of the Administrative Practitioners Bill was introduced in a form which, with a few changes, would be acceptable to the Institute since it would not impair the rights of CPAs to practice before federal agencies.

Carl McFarland, chairman of the administrative law section of the American Bar Association, was the main supporter of the bill. After discussion with an Institute representative, Mr. McFarland agreed to the few changes which the Institute suggested. Conferences were also held with the bill's sponsor in Congress, Congressman Francis E. Walter, who acquiesced in the changes. One item of controversy was thus eliminated.

However, a new bill to make the Tax Court a court of record was also introduced. Efforts by the Institute to include amendments which would maintain the right of CPAs to file petitions before the Tax Court were unsuccessful. Institute representatives, therefore, appeared at hearings and opposed enactment of the bill unless such amendments were made. While the Judiciary Committee of the Senate reported the bill favorably, it was not acted upon by Congress.

Since the filing of petitions with the Tax Court was considered a necessary step in many cases toward a reasonable and prompt settlement of tax controversies in the Bureau of Internal Revenue, the Institute gave thought to other possible arrangements in the event that the Tax Court finally became a part of the federal judiciary.

The House Ways and Means Committee, as the originator of all tax legislation, was naturally interested in arrangements for representation of taxpayers and settlement of tax controversies. The Tax Court problem was therefore discussed with Congressman Wilbur Mills, the chairman of that powerful committee.

As a result, Congressman Mills introduced a bill providing for the creation of an independent tax settlement board, empowered to settle controversies between taxpayers and the

Bureau of Internal Revenue on a completely informal basis, without the necessity of litigation. The Tax Court would remain as a channel which taxpayers could choose for formal proceedings.

Resumption of the National Conference

At the March meeting of representatives of the two national groups in Washington, Mr. Randall, Mr. McFarland, and Messrs. Hamel, Kilpatrick, and Miller of the tax section of the American Bar Association were present. All the issues between the two professions were discussed.

There was agreement by both groups on the pending Administrative Practitioners Bill with the changes made at the suggestion of the Institute.

It was agreed to disagree on the Tax Court bill, though without acrimony. The lawyers made it plain that they could not accept the Mills bill providing for an independent tax settlement board.

It was proposed that the National Conference of Lawyers and Certified Public Accountants might resume effective activity if the Bar representatives could include at least two representatives of the tax section. Mr. Randall promised to consider this suggestion.

After interim correspondence another meeting of the informal group was held in June 1949. There it was agreed that the National Conference should be reactivated following the annual meeting of the American Bar Association in the fall, that those to be appointed to the Conference should be members of the two organizations who had not served actively on the Conference before, and that the tax section and other interested groups in the Bar Association should be represented.

It was also agreed that the National Conference should request local organizations to refrain from litigation or legis-

lation hostile to either profession until the conference groups had an opportunity to consider any dispute.

There was discussion of procedures in the pretrial settlements of tax controversies which might protect the status of CPAs, and remove their opposition to inclusion of the Tax Court in the federal judiciary.

At a third informal meeting of the same group in August it was suggested that a comprehensive statement be developed, defining the area of agreement by the members of the reactivated Conference on what normally constituted the proper scope of activity of accountants and lawyers in the tax field—and that controversial questions on which agreement could not be reached be deferred for later consideration.

Following the annual meetings of the two national organizations in the fall of 1949, the National Conference was reactivated.

Three of the five lawyer members were present or former members of the unauthorized practice committee, including Mr. Randall and David Maxwell who, in the meantime, had served as president of the American Bar Association. He was named co-chairman of the Conference.

Percy Brundage, then senior partner of Price Waterhouse & Co., who had just completed his term as president of the Institute, was the other co-chairman.

A Statement of Principles

The first meeting of the reactivated Conference was held in New York, December 19, 1949. All ten members were present. A news release was agreed upon and issued to the press, announcing the activities of the Conference and its intention to formulate a statement of principles to serve as a guide in disposing of disputes.

The *Conway* case in Minnesota, in which the Minnesota Society of Certified Public Accountants had intervened, with

the encouragement of the Institute, was still before the courts. At this December meeting it was decided that the case had gone too far for the Conference to intervene. This may have been an unfortunate decision, since the case was to cause more trouble later.

There was calm and friendly discussion of the several current issues on which there had been disagreement, but it was agreed that before attempting to deal with them an effort should be made to formulate a broad statement of principles governing relationships between the two professions.

Such a statement was drafted by a subcommittee in the early spring of 1950, and after two days of editing and revision in April the National Conference approved it without dissenting vote. The co-chairmen were asked to seek approval of the Council of the Institute and the House of Delegates of the Bar Association.

In essence, the statement in its preamble said that lawyers and CPAs were members of professions whose services were necessary to business and that, while legal implications and accounting aspects of business problems were separate, legal and accounting phases were often so interrelated that they were difficult to distinguish, particularly in the field of income taxation. For the guidance of both professions the Conference recommended six principles, which boiled down to the following:

1. It was in the public interest that assistance in federal income-tax matters be rendered by lawyers and certified public accountants, while each profession should encourage clients to seek the advice of members of the other on proper occasions.

2. Either lawyers or certified public accountants could properly prepare federal income-tax returns; however, when questions of law or accountancy arose the respective practitioner should suggest the retention of a member of the other profession.

3. Many proposed transactions involved the necessity of ascertaining probable tax effects, and also required the appli-

cation of legal principles: in such transactions the taxpayer was best served by utilizing the joint skills of both a lawyer and a CPA. Only lawyers should prepare legal documents, or give advice on legal matters, or take the steps necessary to create or dissolve different forms of business organizations. Accountants should not describe themselves as tax consultants or tax experts, as lawyers were already prohibited from doing by their canons of ethics.

4. Both lawyers and CPAs were entitled to practice before the Treasury Department, but if in the course of such proceedings questions arose involving the application of legal or accounting principles the respective practitioner should recommend retention of a member of the other profession.

5. Under existing Tax Court rules, non-lawyers could be admitted to practice, but in the interest of taxpayers the advice of a lawyer should be sought when a formal notice of deficiency was issued by the Commissioner, since a choice of legal remedies was then afforded the taxpayers.

6. Claims for refund might be prepared by members of either profession, provided that where a controversial legal issue was involved, or the claim was to be made the basis of litigation, the services of a lawyer should be obtained.

The conclusion of the statement said that it was intended to be tentative, subject to revision and amplification in the light of experience. It was recommended that local co-operative committees or conferences patterned after the National Conference should be organized in the several states.

This statement was submitted, discussed, and approved at a meeting of the Council of the Institute a few days later.

On reference to the Board of Governors of the American Bar Association, however, portions of the statement were questioned by members of the committee on unauthorized practice of the law. A subcommittee of the Board of Governors studied it during the summer, and then recommended that it be referred back to the Conference for reconsideration of the passage dealing with tax advice.

The Conference reconvened on February 8, 1951. Mr. Randall had again been appointed co-chairman for the Bar Association, succeeding Mr. Maxwell.

After lengthy discussion, there was unanimous agreement on substitute language for the paragraphs in the joint statement dealing with tax advice. The new language, in effect, stated that lawyers and CPAs were often asked about the probable tax effects of transactions, and that determination of tax effects frequently was within the function of either the CPA or the lawyer; however, when problems arose which raised uncertainties as to the interpretation of law (both tax law and general law), or uncertainties as to the application of law to the transactions involved, the taxpayer should enlist the services of a lawyer; when the case involved questions of classifying and summarizing transactions in a significant manner in terms of money, or interpreting the financial results thereof, a certified public accountant should be retained; in many cases the skills of both professions would best serve the public interest.

The group also agreed on a new section providing that when a CPA learned that his client was being specially investigated for possible criminal violation of the income-tax law, he should advise the client to seek the aid of a lawyer.

The revised statement was approved first by the House of Delegates of the American Bar Association, and then by the Council of the Institute in the spring of 1951.

Hostilities Not Eliminated

While the Statement of Principles was being hammered out, the trial court in Minnesota held Conway guilty of the unauthorized practice of law in giving tax advice, and granted the injunction requested by the Ramsey County Bar Association.

Conway appealed to the Supreme Court of Minnesota. While Conway was not a CPA, the executive committee of the Institute decided that an effort must be made to persuade

the Minnesota Supreme Court not to decide the case in such broad terms that the legitimate activities of certified public accountants would be curtailed. With the permission of the court, counsel for the Institute filed an *amicus* brief directed to this end.

Thereupon the American Bar Association intervened as another friend of the court and filed a brief supporting the local bar association. The state society and state bar association had already entered the case.

The sweeping arguments in the American Bar Association brief apparently ignored the positions tentatively reached by the National Conference of Lawyers and Certified Public Accountants, and if sustained, could result in severe limitation of the CPAs' tax practice.

The 1950 annual report of the national committee on unauthorized practice of law, while it mentioned rather briefly the reactivation of the National Conference, also had a militant tone. Triumphant reference was made to the *Bercu* case as a landmark in the move to prevent the practice of law by unauthorized and unqualified persons—this, despite the fact that Bercu was a CPA. The intervention of the Institute, it was said, had given the case national significance and delimited the accountants' permissible field of activities even outside of New York.

The report also made favorable reference to the decision of the trial court in the *Conway* case. It was said to have determined that interpretation of income-tax laws, rules and regulations, and court decisions was the exclusive field of those licensed to practice law. Income-tax returns involving questions of law alone or law and accounting combined, it was said, were indicated by this decision as within the field of the lawyer. The report was signed by John D. Randall, chairman, and other members of the unauthorized practice committee.

The tone of the report was discouraging to the Institute members of the National Conference, of which Mr. Randall was a member.

In Massachusetts and the District of Columbia, local boards

of tax appeals had amended their rules so as to exclude CPAs from practice before them.

The concern among accountants was growing into alarm. The Institute organized a "task force," consisting of the chairmen of the committees on federal taxation and relations with the Bar, with three members of the executive committee. This group was authorized to take prompt action in case of emergency, without necessarily awaiting meetings of the executive committee or the Council. This step was considered necessary because the many fronts on which tax-practice problems were arising—in the courts, in Congress, in the Treasury Department, in the states, and in the American Bar Association—required continuous, co-ordinated attention and prompt decision-making ability.

Mathias Correa, who had fought the *Bercu* case for the New York State Society, was retained as special counsel by the Institute in addition to its regular counsel, Covington & Burling, in Washington.

The December 1951 issue of the *Unauthorized Practice News* contained an article entitled, "Co-operation Between Lawyers and Accountants in Tax Practice" by Edwin M. Otterbourg, a former member of the National Conference, which said, in part:

> It was because both certified public accountants and public accountants assumed the right to engage in the general practice of tax law that the *Bercu* and *Conway* litigations were instituted. . . .
>
> The accountants refused to recognize that the well-settled principles of what constitutes unauthorized practice of law. . . should be applied in the tax field.
>
> At long last the American Institute of Accountants. . . grudgingly conceded that the foregoing was true in the income-tax field. This completely disposed of the felicitous argument that "tax accounting" depended merely on a certified public accountant's knowledge of "accepted accounting principles."

Other speeches and articles by lawyers accused accountants of practicing law. The Institute's leaders feared that local bar associations would be encouraged to attack certified public accountants on a broad front.

The gravity of the situation was reflected in Percival Brundage's report to the Council, as co-chairman of the National Conference, in April 1952. He said, "Many lawyers find no difficulty in persuading themselves that the bulk of tax practice consists of legal services which should be performed by lawyers. Extremists in the legal profession publicly lay claim to virtually the entire field of federal income-tax practice as the exclusive domain of the lawyers, conceding only that certified public accountants may prepare simple income-tax returns and perform the other accounting services necessary in connection with income-tax practice under the general supervision of the lawyer. Fortunately, there are more moderate views in the legal profession. . . ."

Referring to the National Conference's Statement of Principles, Mr. Brundage said, "This document does not answer many of the specific questions which have been debated, but it does, nevertheless, accomplish several other important things." He stressed the recognition that both professions had a legitimate place in the tax field, and that questions of law and accounting in federal income tax were interwoven and overlapping. He continued, "The statement leaves virtually untouched, however, the core of the controversy, which is the question whether the determination of specific items of income and expense is essentially a matter of accounting regardless of the extent to which statutory rules, regulations, or judicial decisions must be observed in such determinations . . . or whether the application of law for any purpose, including the determination of taxable income, is essentially the practice of law. . . . This question will probably have to be resolved sooner or later. . . ."

Mr. Brundage also reminded the Council that local bar associations might initiate punitive actions against CPAs if they so desired, as in the *Loeb, Bercu,* and *Conway* cases, and that state and local courts, "which almost by definition cannot be expected to have an intimate understanding of federal income-tax matters," would find it difficult to understand the

CPA's position, and thus might easily be persuaded that the income-tax field was essentially a field of law.

However, he questioned whether state and local courts had jurisdiction over federal tax practice: "They have dealt with it on the assumption that the practice of law is subject to state regulation, but there are very solid grounds for the belief that the federal courts might hold that the scope of activity of an agent enrolled to practice before the Treasury Department, in a matter involving collection of the federal revenues, is a matter of federal jurisdiction."

While strongly advocating a sincere co-operative effort to reach an amicable solution of the difficulties by direct negotiations with the Bar, Mr. Brundage recognized that if the views of the more belligerent lawyers prevailed the accounting profession must take whatever action was possible in self-defense—if necessary, to take the controversy to the business public, the taxpayers, who in any case must foot the bill. The importance of maintaining good communications with the Bureau of Internal Revenue, the Treasury Department, its committee on practice, and the appropriate members of Congress was also emphasized.

Another Crisis in the Conference

In 1952 and 1953 the National Conference continued to meet. It considered a number of cases involving fee litigation in tax matters and resolved several of these situations. It came to agreement on several peripheral policy questions. It reported in 1953 that in 19 states local conference groups or other co-operative relationships between lawyers and CPAs had been established.

The National Conference was actively supporting the Administrative Practitioners Bill in Congress—as revised in accordance with the Institute's suggestions.

At a meeting of the Conference in October 1953, however,

a cloud no bigger than a man's hand crossed the horizon. The lawyers asked the accountants' interpretation of the phrase in the Statement of Principles, "uncertainties as to the interpretation of law (both tax law and general law) or uncertainties as to the application of law to the transaction involved. . . ." The accountants interpreted the phrase to mean uncertainties of tax law in the sense of purely legal subject matter as distinguished from subject matter involved in determination of income to be taxed.

The lawyer members of the Conference disagreed. They suggested that the quoted portion of the Statement of Principles conveyed an entirely different meaning to lawyers generally. A subcommittee was appointed to consider the possibility of interpreting or amending this part of the Statement.

A Change of Policy

John W. Queenan, one of the top partners of Haskins & Sells, succeeded Mr. Brundage as co-chairman of the National Conference.

At the meeting of Council in the spring of 1954 Mr. Queenan reported soberly on several ominous developments. The pressure for clarification of the controversial section of the Statement of Principles had become more insistent. The lawyer members of the Conference were urging further concessions which the Institute representatives were not disposed to make.

In the past year unauthorized practice committees in Rhode Island, California, and Florida had launched attacks—two of them in court, one of them by threat—on three major areas of tax practice by non-lawyers: preparation of federal income-tax returns, representation of taxpayers before the Internal Revenue Service, and practice before the Tax Court. The possibility was foreseen that continuous efforts would be made to chip away the CPAs' tax practice through state court decisions—each case being cited as authority in another, and each

going a little further in curtailing the tax practice of non-lawyers.

"It seems doubtful," Mr. Queenan's report said, "whether this trend of adverse decisions in state courts can be checked in the long run by purely defensive action in every case in every state where the bar associations may choose to attack." It was suggested that the only effective solution would be to have the federal government clearly assume jurisdiction over federal tax practice.

To this end, it was reported, the Institute had proposed to the Treasury Department elimination or modification of the section of Circular 230 which provided that ". . . nothing in the regulations in this part shall be construed as authorizing persons not members of the Bar to practice law." This provision had been cited by Bar Association spokesmen as meaning that non-lawyers enrolled to practice before the Treasury could not perform work which the state courts had decided constituted the practice of law. It was noted that the American Bar Association had already indicated its intention of opposing the change in Circular 230 recommended by the Institute.

Federal legislation to solve the problem was also suggested as a possibility.

It was also reported that a new draft of an Administrative Practitioners Bill had been prepared by the administrative law section of the American Bar Association, which ignored completely the agreements made several years before, resulting in elimination of provisions objectionable to the Institute. The new bill was dangerous in many particulars. Efforts to have it modified through negotiations had failed, and the Institute had been notified that the bill would probably be introduced at an early date.

The immediate question posed to the Council was whether it was time for the Institute to take its case to the public, in spite of reluctance to exacerbate the situation. It was recognized that an appeal for public support might provoke retaliatory actions on the part of the Bar Association.

Nonetheless, the Council, after extensive debate, approved

an aggressive program to inform clients, friendly lawyers, and other interested segments of the public of the accountant's side of the controversy, and to resist by all possible means legislation that might limit the legitimate activities of CPAs in tax practice.

Soon after, the prestigious public-relations firm of Earl Newsom & Company was retained to assist the Institute in carrying out the approved program.

Arthur B. Foye, senior partner of Haskins & Sells, was then president of the Institute. He co-ordinated the activities of the "task force" with those of Mr. Correa as legal counsel, Mr. Newsom as public relations counsel, and the executive director of the Institute, in carrying out the new program.

The Agran *Case*

One month after Mr. Queenan had reported to the Council, the Superior Court, County of Los Angeles, California, handed down a decision in the case of *Reuben Agran, CPA* v. *Morris Shapiro et al.* Agran had sued for a $2,000 fee for services rendered in a tax matter, and the Municipal Court in Los Angeles had ruled in his favor. The defendants had appealed to the Superior Court, contending that Agran had illegally practiced law without a license.

Agran was a CPA, which distinguished his case from the *Conway* case, and was enrolled to practice before the Treasury Department. Shapiro was a regular client, whose tax return Agran had prepared, which distinguished his case from the *Bercu* case. The service in question consisted of an informal settlement with the Internal Revenue Service involving a loss-carryback adjustment, which could hardly be considered a substantive legal question. Nevertheless, the Superior Court held that Agran had practiced law.

Most alarming to the accounting profession was the court's

citation of the controversial section of the Statement of Principles recommended by the National Conference and approved by the Council of the Institute in 1951. The court held that the plaintiff undertook to determine the tax effect of the defendant's transaction, the ascertainment of which involved "uncertainties" both as to the interpretation of the tax law and the application thereof to the transaction in question. This the court viewed as the practice of law, and noted that Treasury Department Circular No. 230 did not authorize non-lawyer agents to engage in such practice.

The net effect of this decision seemed to be that a CPA in Los Angeles County was engaged in unlawful activities when he rendered services which the United States Treasury Department had specifically authorized him to render.

From the Institute's point of view, this was the last straw.

Appeal to the Treasury Department

A conference was arranged in July 1954, with the Secretary of the Treasury, George Humphrey. The Under Secretary of the Treasury, Marion Folsom, and a member of the Treasury counsel's office were also present. President Foye headed the Institute's delegation.

Mr. Foye explained that Treasury Department Circular No. 230 gave accountants enrolled to practice before the Treasury the right to represent clients in tax settlements. The *Agran* decision took that right away from an enrolled agent. The only basis for the *Agran* decision was an interpretation of the ambiguous provision of Circular No. 230, that nothing therein was intended to give non-lawyers the right to practice law. It appeared that there was a need to clarify the meaning of that section.

After questioning by the Secretary of the Treasury and further discussion, he requested a brief written statement of what the Institute regarded as the proper scope of enrolled agents

in tax practice, and invited the group to discuss the matter later with Under Secretary Folsom.

Soon afterward Mr. Foye submitted a one-page statement of the proper scope of accountants' tax practice before the Treasury Department. A recommendation for amendment of the ambiguous section of Circular No. 230 was also submitted to Under Secretary Folsom.

Appeal to Congress

Further legal proceedings in the *Agran* case were expected. The *Conway* case had been decided by the Minnesota Supreme Court in favor of the local bar association.

The Institute had announced its intention to oppose the new form of Administrative Practitioners Bill, supported by the American Bar Association, until the objectionable provisions could be eliminated.

The National Conference had been unable to agree on an interpretation of the controversial section of the Statement of Principles relating to tax effects of transactions.

The Institute's executive committee concluded that a chaotic situation could be averted permanently only by Congressional action. After discussions of the problem, Congressman Daniel A. Reed of New York, then Chairman of the House Ways and Means Committee, introduced a bill to clarify the responsibility and authority of the Treasury Department to regulate federal tax practice. This bill specifically provided that no one could be deprived of the right to practice before the Department because of his failure to be a member of any profession or calling. In explaining the intent of his bill, Mr. Reed referred to the unfortunate results that would follow curtailment of the role that professional accountants had occupied in tax practice for 40 years.

The House of Delegates of the American Bar Association voted to oppose this bill.

Appeal to the Public

With the expert assistance of public relations counsel, Earl Newsom and his associates, the Institute published a pamphlet entitled "Helping The Taxpayer—A Discussion of Current Issues Affecting Professional Services in the Field of Federal Taxes." This pamphlet was a simple statement of the issues involved in the controversy with the Bar, and the extent to which the public interest was involved. The discussion was illustrated by a graph indicating what happened to federal income-tax returns in 1952: 54,000,000 returns were accepted as filed; 1,200,000 required minor adjustments after mathematical verification or examination; 714,000 required discussion at lower levels of the Internal Revenue Service; 35,000 required discussion at intermediate levels of the Revenue Service; 9,400 required discussion at upper levels of the Revenue Service; 1,200 cases were decided in the Tax Court; 636 cases were decided in actual courts of law.

This pamphlet was distributed to all members of the Institute, who were offered free copies for distribution to clients and friends, businessmen and influential acquaintances. Two hundred thousand copies were so distributed. Recipients included deans of law schools, key members of Congress, selected government officials, and editors.

Later, a fifteen-minute documentary motion picture was produced under the same title—"Helping the Taxpayer"—illustrating what certified public accountants actually did in tax practice. It included a scene in which the advice of a lawyer was sought in dealing with a question of general law which arose in connection with a tax case. This film was widely shown.

The pamphlet aroused widespread discussion throughout the country. Many lawyers wrote to the American Bar Association about it.

Among others, Erwin Griswold, Dean of the Harvard Law School, read the pamphlet. He was moved to write a friendly letter to Mr. Foye, as president of the Institute, indicating

regret that the Institute had seen fit to take the controversy to the public, but offering to be of assistance, if he could, in facilitating a settlement of the matter.

At the annual meeting of the Institute in the fall of 1954, Maurice H. Stans, of Chicago, senior partner of Alexander Grant & Company, had been elected president to suceed Mr. Foye. Mr. Stans had been a member of the National Conference. Arrangements were made for him to meet Dean Griswold.

Dean Griswold Acts

At this meeting, Dean Griswold asked a number of challenging questions, but was apparently satisfied by Mr. Stans' responses that the Institute sincerely desired a peaceful settlement of the controversy.

Dean Griswold had accepted an invitation to address the Association of the Bar of the City of New York. He decided to make the tax-practice controversy the subject of his paper. His speech was an even-handed, dispassionate analysis of the current position.

He described the organization of the CPA profession, and suggested that CPAs had earned the right to a position superior to that of non-certified accountants and other non-lawyers in tax practice. He disapproved of the Institute's public-relations activities and its support of federal legislation to establish its position in the tax field. But he expressed the view that there could be no sharp dividing line separating the functions of lawyers and certified public accountants in the tax area. "The two fields clearly overlap," he said. "They shade into one another with no clear line between them. . . . It may well be appropriate for a certified public accountant to do things which would be over the line for another with less status."

This speech was published and was read by many lawyers.

Some months later, in August 1955, Dean Griswold spoke

on the same subject before the tax section of the American Bar Association. His recommendation was to cool the controversy, to return to the Statement of Principles, and to deal with specific problems by friendly negotiation.

He expressed the view that the unauthorized-practice-of-law approach to the tax-practice problem was not a sound approach. "Obviously," he said, "there are many things involving the law and its application which can and must be done by non-lawyers. The practice-of-law formula is not a safe and sound approach, it seems to me, if it is taken to include a rule that any matter involving application of statutes, regulations and court decisions can only be handled by a lawyer." With reference to the *Agran* decision, Dean Griswold expressed the opinion that the court had taken a too literal, or semantic, view of the concept of practice of law.

On the other hand, the Dean raised questions as to the propriety of the activities of accountants in certain situations. However, he observed that in actual practice members of the two professions were experiencing little difficulty in working together, and that the accountants generally had not been limited in the customary scope of their tax activities in actual practice. "This is an area," he said, "where it is extremely difficult to lay down explicit rules."

These speeches and subsequent activities by Dean Griswold, who enjoyed great prestige in legal circles, helped greatly to create a climate conducive to ultimate resolution of the conflict.

Another Effort at Peacemaking

When Maurice Stans was nominated for the presidency of the Institute in the spring of 1954, he talked with Tom Boodell, a fellow Chicagoan, who was then chairman of the unauthorized practice committee of the American Bar Association, about the possibility of resuming friendly discussions on the tax-practice problem.

In the National Conference negotiations had reached an impasse, and the two professions were fighting in the courts, in Washington, and in the area of public opinion. A long-drawn-out period of battle was impending, which was bound to be unpleasant for both sides.

No sooner had Mr. Stans been elected president than he received a congratulatory letter from Loyd Wright, president of the American Bar Association, suggesting a renewal of efforts to resolve the difficulties between the two organizations by negotiation.

The two presidents met in Chicago early in December 1954. Their personal views of the tax-practice problem appeared to be not very far apart. Mr. Wright agreed to ask a newly created Bar Association committee on professional relations, headed by William J. Jameson of Montana, a former judge, to meet with a group of Institute representatives as soon as possible.

This new committee had been appointed by Mr. Wright to try to work out a settlement with the accountants. It included representatives of the tax and administrative law sections of the Bar Association, as well as Mr. Boodell of the unauthorized practice committee.

The Institute was to be represented by a new committee on relations with the Bar, headed by John Queenan, but including four members who had not previously been involved in the controversy.

These two groups, it was assumed, could take a fresh look at the whole problem, unhampered by prejudices or personal antagonisms which might have been developed in the negotiations of earlier years.

The two committees met in Washington on January 25, 1955. Agreement was readily reached on the desirability and practicability of an agreement which would resolve the entire controversy, and both sides felt that the local organizations of each profession could be persuaded to accept such an agreement.

The lawyers agreed without hesitation that the accounting profession had an important role in taxation which was wel-

comed by the Bar and should not be curtailed. This generalization was qualified by an indication that accountants should not invade the field of law, and that the 1951 Statement of Principles should be the criterion.

There was general agreement that CPAs should be permitted to continue to prepare returns and represent taxpayers in proceedings before the Treasury. However, the lawyers felt that CPAs should not practice in the Tax Court. They recognized that below that level it was impossible to draw a clear line between legal and accounting elements of tax practice.

There appeared to be agreement that it was necessary for CPAs to interpret and apply the Internal Revenue Code and related regulations and court decisions. However, the lawyers cautioned that there were many matters in which CPAs should not operate alone, and on which lawyers should be brought into collaboration.

There appeared to be agreement that Circular No. 230 could be amended to protect the rights of CPAs to practice before the Treasury Department without limitation. However, the lawyers felt that this should be done without eliminating the proviso prohibiting non-lawyers from practicing law.

The Institute representatives agreed that legislation along the lines of the Reed Bill would be unnecessary if Circular No. 230 could be amended satisfactorily.

Both sides felt that joint machinery established by the two professions could resolve any confusion as to the purpose and interpretation of the Statement of Principles.

The Institute's representatives agreed to support legislation which would make the Tax Court a court of record if CPAs presently enrolled to practice before the Court were protected by a grandfather clause.

There was no objection to a reaffirmation of the Statement of Principles, if it was understood that it did not define the limits of the practice of accounting or the practice of law, and was not intended to be used in court proceedings as had been done in the *Agran* case.

The two groups agreed to support an administrative practi-

tioners bill along the lines of the earlier Walter Bill, without the troublesome proviso included in the pending bill that no one not a lawyer should be authorized to practice law.

The next step was to draft an agreement covering all points discussed, and place this agreement before the Board of Governors of the Bar Association on February 19 and the House of Delegates on February 21. A subcommittee was appointed to draft the agreement.

During the following few weeks, under intense pressure, the subcommittee, with the assistance of its colleagues, developed successive drafts of such an agreement.

Meanwhile, the Under Secretary of the Treasury had been advised that the two organizations were making a sincere effort to reconcile their differences.

The efforts to develop precise language reflecting the general agreements continued right up to the eve of a meeting of the two negotiating groups scheduled for February 18 in Chicago, where the Bar Association's House of Delegates was to meet three days later.

At that meeting it was impossible to get full agreement on precise language. The effort continued through the next day. With each successive draft the proposed statement became shorter, in an effort to eliminate controversial language and to deal only with the essential elements of the problem. The final effort consisted of four short paragraphs stating, in effect, that both sides reaffirmed the Statement of Principles with the understanding that it was not a definition of the practice of law or accounting, and was not intended to be used in adversary proceedings; that the Tax Court should become part of the judicial system, but that non-lawyers already admitted to practice before it should be permitted to continue; that CPAs were permitted to practice without limitation before the Treasury Department; and that differences between the two professions should be resolved by conference rather than by litigation.

At a final meeting on February 20 it became evident that agreement even on this brief statement was impossible.

Subsequent information indicated that the five members of

the Bar Association's negotiating committee could have readily reached agreement with the Institute's representatives, but had been unable to secure the acquiescence of other influential members of the Bar whom they had felt obliged to consult on the matter.

The Institute's representatives left Chicago with a profound sense of disappointment and discouragement.

Judge Jameson reported on behalf of his committee on professional relations to the House of Delegates of the Bar Association. He said he had hoped to come before the House with a definite agreement for approval. While this had not been possible, he felt that progress had been made. He described the discussions that had been held with representatives of the Institute, and indicated the difficulty of reaching agreements in the somewhat tense atmosphere that had developed, but said that all parties had acted in good faith and that tentative agreements had been reached on a number of matters.

In order not to hamper further negotiations, Judge Jameson said, he would not attempt to explain to the House the areas of agreement or disagreement at this time.

He did, however, discuss the question of what would happen if no agreement were reached: "In that case," he said, "the accountants will press very vigorously for the enactment of these two bills that are now pending in Congress. . . . They have accumulated a substantial fund for that purpose. In fairness to the accountants, I should say they are not using that fund as a threat or anything of that kind, but we know they do have a very substantial sum of money to spend for that purpose. We can't hope to match that in the event we get into this controversy. What does that mean? It means we have to spend some money, of course. . . . We hope that won't be necessary. . . . I think it would be, and I know all the members of the committee agree, a serious mistake from the standpoint of both professions, as well as the public, if we do have to get into this controversy."

He proposed that the special committee be continued, and authorized to continue negotiations with the American Insti-

tute of Accountants and others with respect to problems arising in tax practice. A resolution to this effect was adopted by the House of Delegates.

In April 1955, the Institute's new committee on relations with the Bar, which had conducted the negotiations with Judge Jameson's committee, reported to the Council. The report said, "At the close of the first joint meeting on January 25 the way seemed clear for reasonably early settlement of any differences between the two professions. Efforts to draft a document, however, which would incorporate the points of agreement reached at the first meeting were unsuccessful." The report went on to say that after further meetings it became clear to the Institute representatives that settlement of the differences by mutual agreement had little chance of success at that time. "The two groups failed to reach an accord," the report said, "on the issue which the Institute representatives considered basic to any overall agreement, namely, clarification of Treasury Department Circular No. 230 so as to make it plain that certified public accountants may continue to practice before the Treasury Department as they have done for 40 years." However, it was stated that the discussions had contributed to a better understanding of the respective viewpoints, and that the way was clear for resumption of discussions if either group should wish to offer a fresh approach to the problem.

At the same meeting of Council a special committee on tax practice, headed by Arthur Foye, which had replaced the earlier "task force," reviewed the entire situation. The outlook was ominous. The scope of the CPA's tax practice was seriously threatened in several states. The California State Bar had entered the *Agran* case. The new Administrative Practitioners Bill gravely threatened practice by non-lawyers before all government agencies.

While recommending continuation of efforts to negotiate a settlement with the Bar Association, the committee advocated another effort to persuade the Treasury Department to clarify

its regulations to protect the present status of CPAs. If that effort failed, it was proposed to renew the effort to secure federal legislation to the same end. As a last resort a review of the *Agran* case, or some similar case, by the United States Supreme Court might be requested.

The Council approved these recommendations.

The Treasury Acts

Mr. Queenan advised Judge Jameson, his counterpart in the Bar Association, that the Institute was determined to press for a clarification of the CPA's position by amendment of Treasury Department Circular No. 230. Dean Griswold had become a member of Judge Jameson's committee. It was agreed that the two committees would draw up a joint statement outlining the positions of the two organizations with respect to the proposed amendment. Messrs. Jameson and Queenan called on Under Secretary Folsom in May and presented him with this joint statement.

Soon after, H. Chapman Rose succeeded Mr. Folsom as Under Secretary of the Treasury. Under date of August 8, 1955, Mr. Queenan wrote Mr. Rose a lengthy letter reciting the history of the Institute's request for clarification of Circular No. 230, beginning with the meeting with Secretary Humphrey a year before. The letter explained the Institute's position in detail, and the reasons why it had been impossible to reach an agreement with the American Bar Asssociation. Finally the request for clarification of Circular No. 230 was renewed.

Subsequently, Institute representatives met with Mr. Rose and other key Treasury officials to discuss the matter.

Bar Association representatives also conferred with Treasury officials, explaining their position.

The matter came to a head in January 1956. Intensive discussions were held by Under Secretary Rose and associated

Treasury officials with both Institute and Bar Association representatives.

A draft of a clarifying statement which might be made by the Secretary of the Treasury was submitted to both groups. After careful study the Institute's group reported that the statement was wholly acceptable without any change. The Bar Association group found parts of it objectionable and requested an opportunity to review the matter at a meeting of the House of Delegates. The Institute's representatives urged Mr. Rose to request the Secretary to act promptly, predicting that if the matter were submitted to large groups on both sides agreement would be impossible.

On January 30 the Secretary of the Treasury issued a statement which was inserted as a footnote in the appropriate part of Circular No. 230. The statement included the following key assertions: "It is the intention of the Department that all persons enrolled to practice before it be permitted to fully represent their clients before the Department. . . . The Department believes this has been beneficial to the taxpayers and to the government, and that there presently appears no reason why the present scope and type of practice should not continue as it has in the past." Referring to the proviso that nothing in the regulations was to be construed as authorizing persons not members of the Bar to practice law, the Secretary's statement said, "It is not the intention of the Department that this second proviso should be interpreted as prohibiting enrolled agents from fully representing their clients before the Department."

The statement expressed gratification at the co-operative efforts of the legal and accounting professions, as illustrated by the joint Statement of Principles Relating to Practice in the field of Federal Income Taxation. The Secretary's statement concluded with the following:

> The question of Treasury practice will be kept under surveillance so that if at any time the Department finds that the professional responsibilities of its enrolled agents and enrolled attorneys are not being properly carried out or understood, or that the members of

either profession are not respecting the appropriate field of the other, it can review the matter to determine whether it is necessary to amend these provisions of the Circular or take other appropriate action.

In the view of the Institute's legal counsel and its policy-making committees, this statement clearly indicated the Treasury Department's intention to reserve the right to decide what its enrolled agents could and could not do, and for the time being to impose no restriction on the customary practice of enrolled agents, regardless of the findings of state courts.

A basis for resumption of co-operative relations with the American Bar Association was established.

The National Conference Reconstituted

The American Bar Association apparently accepted the Secretary of the Treasury's action as conclusive. Steps were immediately taken to resume meetings of the Institute's committee on relations with the Bar and the Bar Association's committee on professional relations. By September 1956 the two committees had drafted a joint statement reiterating support for the Statement of Principles and proposing machinery to resolve differences that might arise.

By April 1957 the National Conference of Lawyers and Certified Public Accountants had been reconstituted, with the membership of the two co-operating committees as members. Agreement had been reached on a joint statement, "The Professional Relations of Lawyers and Certified Public Accountants," which had been printed and widely circulated. This joint report included the text of the Treasury Department's interpretation of Circular No. 230, and the text of the Statement of Principles. Copies were circulated among state societies of CPAs, and state and local bar associations. Specific questions coming before the Conference group had been settled without diffi-

culty. Efforts were made to have local associations of both professions adopt and approve the Statement of Principles without change.

Peace and tranquility were being restored. Tensions were being relaxed. An atmosphere of mutual confidence and co-operation was being created.

John Queenan, who had been chairman of the Institute's delegation through the delicate negotiations of 1954-55, and had maintained cordial personal relations with Judge Jameson as chairman of the Bar's committee on professional relations, continued as co-chairman of the Conference representing the Institute until 1961, when he was elected president of the Institute. He was then succeeded by Thomas D. Flynn. Judge Jameson retired as co-chairman representing the Bar Association in 1959, when he was succeeded by Dean Griswold, whose attitude throughout had been judicial and friendly.

The National Conference was influential in settling controversies which arose in a number of states, either through threatened suits to enjoin accountants from the unauthorized practice of the law, or through suits by CPAs for fees which were defended on the ground of unauthorized practice. The lawyer-members of the National Conference were influential in dissuading some state or local bar associations from intended hostile actions against the accounting profession. Gradually incidents of this nature ceased, and the situation became stabilized throughout the country.

One source of continuing irritation to members of the Bar was the employment of lawyers by accounting firms. It was widely suspected—and Dean Griswold in his speeches had echoed the feeling of many lawyers—that lawyers on the staff of accounting firms were permitted to do legal work for clients.

After discussion of this problem the Institute representatives of the National Conference agreed that lawyers employed by accounting firms should not be permitted to do anything that the firms were not permitted to do.

In 1958, the Institute affirmed this position by adopting a new rule of professional conduct reading, "A member in his

practice of public accounting shall not permit an employee to perform for the member's clients any services which the member himself or his firm is not permitted to perform."

The Tax Court

Another question of continuing discussion was the status of the Tax Court. The Bar Association strongly supported transfer of this body to the Judiciary. The Institute maintained the position that it would support such a measure if certified public accountants already admitted to practice before the Court were permitted to continue under a grandfather clause, or, alternatively, if an informal tax settlement board were created before which certified public accountants might represent their clients.

In 1968 the Institute's Council resolved to support the transfer of the Tax Court to the Judiciary provided CPAs already admitted to practice would be permitted to continue, and provided that if a small claims division of the Tax Court were created, as had been suggested, CPAs would be permitted to practice before it.

Administrative Practice Legislation

The Institute had been instrumental in blocking a series of bills supported by the American Bar Association relating to practice before administrative agencies of the federal government. The main thrust of these bills was to permit lawyers in good standing in their own states to represent their clients before any federal administrative agency without special enrollment. Most of these bills also contained provision for representation by non-lawyers under specified circumstances, but sometimes subject to restrictions which might have handicapped

CPAs in their tax practice or in informal representation before other agencies.

Another bill of this type was introduced in 1964. Bar representatives were unwilling to make changes which would satisfy the Institute, and Institute representatives were obliged to oppose the bill at hearings before the Committee on the Judiciary of the House of Representatives. The state societies of certified public accountants strongly supported the Institute's position by communication with their own Congressmen. The proposed legislation failed to pass.

However, similar legislation was introduced with the support of the Bar in 1965.

Efforts were made by the Institute to reach agreement with the Bar Association on amendments which would protect the CPAs' position before the Treasury Department and other agencies, but without success.

The critical hour was approaching. The Congressional committees were preparing their reports on the bill.

On August 30, 1965, Thomas D. Flynn, then president of the Institute, and the executive director met privately with counsel for the subcommittee of the Senate Judiciary Committee which had this bill in charge. After explaining the reasons for the Institute's position, Mr. Flynn stated that if the bill were amended to provide specifically that certified public accountants were entitled to practice before the Treasury Department, the Institute would support the legislation, and would do everything possible to neutralize any opposition from other quarters. However, he said that if such an amendment were not adopted the Institute would have no choice but to mobilize all its resources in opposition to the bill.

The response was that if the Bar Association would agree to such an amendment it would be included.

Mr. Flynn immediately telephoned the president of the American Bar Association, who consulted his associates and then informed Mr. Flynn that the American Bar Association would not object to the inclusion of the desired amendment.

On September 13, Institute representatives met with the president, the executive director, and other representatives of the Bar Association in Washington. Agreement was reached on the precise language of the proposed amendment. The entire group then met with Representative Willis of Louisiana, the sponsor of the House version of the bill, who agreed to accept the amendment on which the two groups had come to a meeting of the minds. On September 15, the Senate Judiciary Committee approved the bill, including the Institute's amendment. On September 23, the Willis subcommittee of the House ordered the bill favorably reported with the Institute's amendment. The bill passed both houses of Congress and was designated as Public Law 89-332. It contained the following provision, inserted as an amendment at the Institute's request:

> Any person who is duly qualified to practice as a certified public accountant in any state, possession, territory, commonwealth, or the District of Columbia may represent others before the Internal Revenue Service of the Treasury Department upon filing with that agency a written declaration that he is currently qualified as provided by this sub-section and is authorized to represent the particular party in whose behalf he acts.

Thus, after a struggle lasting over decades the status of CPAs in practice before the Treasury Department was confirmed specifically in a federal statute.

In the end, after 30 years of controversy, the Treasury Department and the Congress had settled the matter. The authority of CPAs in the tax field was firmly established. But this might not have happened if the organized Bar had offered massive resistance. It is a tribute to the restraint, the objectivity, and the fairness of those leaders of the legal profession who undertook to referee the controversy that no such massive resistance developed. To those distinguished members of the Bar the accounting profession is deeply indebted.

CHAPTER 10

Education and Experience

ONE OF the first concerns of the organized accounting profession in the United States was the training of candidates. The American accountants had no authority to require apprenticeship training of the sort prevailing in Great Britain, where the Institutes of Chartered Accountants were accrediting agencies ("qualifying bodies"). The only alternative seemed to be formal education plus experience in public accounting.

The Institute's predecessor, the American Association, attempted to establish its own school of accounting, but failed. More success attended subsequent efforts to encourage colleges and universities to introduce courses in accounting. The numbers of educational institutions offering such courses increased rapidly, but the scope, nature, and level of these courses varied widely. There was nothing the national professional organization could do about it except advise and exhort.

Since control of requirements for the CPA certificate was in the hands of the respective state boards of accountancy, preliminary requirements for the certificate also varied widely.

For decades the emphasis was on experience. It was not until the 1930's that New York introduced the first requirement of college education as a prerequisite for the CPA certificate. Then it seemed necessary to define the kind of college education that would be acceptable, which the New York authorities did by specifying courses to be taken and hours to be devoted to them.

Foreseeing similar developments in other states, the Institute's committee on education thought it would be helpful to set up standards of education at the national level, which might encourage uniformity throughout the country.

In 1937 the chairman of this committee was Professor Roy B. Kester of Columbia University, an accounting teacher of great prestige and author of a well-known textbook on accounting.

Proposed Educational Standards

The committee's 1937 report proposed that the Institute (1) endorse four years of collegiate training as a minimum educational requirement for professional practice, with a specified number of hours devoted to professional subjects; (2) formulate standards covering courses and their content, faculty personnel, library and laboratory equipment, and financial resources—these standards to be used as a basis for rating the schools offering professional training in accountancy; (3) encourage amendment of the state accountancy laws to introduce higher educational requirements for the CPA certificate; and (4) broaden the CPA examination in accordance with the suggested program.

One member of the committee submitted a minority report, objecting to the effort to put accounting curricula in a "strait-jacket," and also to the proposal that the Institute accredit educational institutions.

However, the report was submitted to the executive com-

mittee, which proposed to the Council a resolution endorsing the majority recommendations. The Council debated the matter at length. The resolution was amended in some respects, and finally was adopted with four members being recorded as voting in the negative. The substance of the resolution was as follows:

1. That the Council favored the highest practicable standards of preliminary education, similar to those effective in other professions, such as law or medicine;
2. That desirable standards were completion of a full course in a college of liberal arts plus graduate work in accounting;
3. That the Council favored college courses specifically designed to train students for public accounting practice, and approved the suggestions of the committee on education as to cultural and professional subjects to be included in such courses;
4. That the committee be instructed to develop standards by means of which the Council might judge whether courses in any given educational institution met with its approval;
5. That the CPA certificate should be available to candidates lacking formal education who met high standards of apprenticeship training; and
6. That additional experience should be required of applicants for the CPA certificate who had not completed satisfactory courses in accountancy of collegiate grade.

The committee on education was delighted with this reception. It proceeded to analyze the catalogues of schools which were members of the American Association of Collegiate Schools of Business. A questionnaire was also sent to the deans of these schools to obtain supplemental information.

By 1940, however, resistance to the committee's program was developing. Many deans and accounting professors, including influential members of the American Accounting

Association, objected to the Institute's proposal to develop detailed curricula and standards for accreditation of accounting courses in the business schools.

Some practitioners also objected to the committee's approach, but for different reasons. They felt that too little emphasis was being placed on technical training, and too much on "cultural" subjects.

From both dissident quarters there were rumblings of discontent at the Council meeting in the spring of 1940.

Meanwhile, efforts were being made through other channels to strengthen the Institute's relations with the American Accounting Association, representing the academic branch of the profession. Several members of the Institute's executive committee met with representatives of the Association in December 1939 for informal discussion of common problems and the possibility of closer co-operation. Among the topics of discussion were the CPA examinations, accounting education, and accounting research. Thereafter the president of the Association was invited to attend the spring meetings of the Council of the Institute.

The executive committee then decided that, before the committee on education published a list of schools meeting the curriculum standards which the Council had approved, an effort should be made to reach agreement with the American Accounting Association on such standards and that deans of schools of business should be given notice at least a year before publication of such a list. In these decisions, the committee on education gracefully acquiesced.

In 1941, T. Edward Ross, one of the founding partners of Lybrand, Ross Bros. & Montgomery in Philadelphia, succeeded Professor Kester as chairman of the education committee.

Mr. Ross arranged a meeting in Detroit in September 1941, which was attended by representatives of the American Accounting Association, the American Association of Collegiate Schools of Business, and the Institute's education committee. A complete stenographic transcript of the discussion was made.

At this meeting it was concluded that the establishment of minimum standards for accounting education would be very difficult, partly because of the differences of opinion among educators about the emphasis which should be placed on professional subjects as contrasted with general cultural studies.

It was agreed that, at the stage of development which both accounting practice and accounting education had then reached, the most useful service which the Institute's education committee could perform was to report to educators the experience of practitioners in employing graduates of various types of accounting courses, and that the pedagogical problem of preparing and adjusting courses of study to meet the profession's requirements should be left to the educators.

To emphasize its determination not to meddle in pedagogical affairs, the executive committee decided in 1944 that the Institute's committee on education should be composed entirely of practicing accountants, rather than including educators as in the past. Co-operation between practitioners and educators was expected to be accomplished by working with a corresponding committee of the American Accounting Association.

The new chairman of the Institute's committee on education was the same John W. Queenan who later played so prominent a part in the events described in Chapter 9.

The previous educational program of the Institute, aimed at uniform standards, was abandoned. A new program of joint action by the Institute and the American Accounting Association was presented, with emphasis on what the Institute could do to help the teachers; for example, by providing instructors with records of actual cases in auditing, by providing special training for war veterans, by accepting students as interns for a quarter of their collegiate year, by giving younger accounting instructors an opportunity to obtain public accounting experience, by developing staff-training programs, and by encouraging students to prepare for the accounting profession. To implement the latter suggestion a revision was undertaken of the pamphlet "Accountancy is a Career for

Educated Men," which the Institute had issued in 1926 as a recruiting device.

Matters of curriculum and teaching methods were left completely in the hands of the academic fraternity.

The numbers of college graduates entering the profession were increasing. The diversity of educational backgrounds, however, was marked. Many of the candidates were liberal arts majors, and many others were science or engineering majors. Less than half, it was estimated, were accounting majors.

From 1945 to 1951, the Institute's committees on education concerned themselves mainly with internship programs, on which a booklet was published in 1949; the possibility of staff-training programs, on which no progress was made until much later; and the encouragement of graduate-study conferences at the major universities.

The idea of the graduate-study conference had originated with Percival F. Brundage. He had been invited to lecture at the Oxford Summer Course sponsored by the Institute of Chartered Accountants in England and Wales, and was so well impressed with the proceedings that he recommended arrangement of similar courses in the United States. These courses were restricted to a specified number of individuals, and consisted of lectures, followed by discussion in small groups over a period of several days. The first American graduate-study conference took place at the University of Michigan in 1948, followed soon by similar conferences at Harvard, Stanford, Rutgers, Louisiana Polytechnic Institute, the universities of Maryland and Wisconsin, and later at a number of other institutions.

The conferences proved most useful as refresher courses for CPAs in practice, most of them partners of accounting firms or sole proprietors, but the programs in general were not pitched at levels appropriate to staff training.

The American Accounting Association on its own initiative labored for several years on the development of rating standards for accounting courses. Its committee on this subject finally published a report recommending roughly an equal

division between cultural and professional subjects at the four-year undergraduate level. The hours to be devoted to specific courses under each classification were indicated.

During this entire period, however, there was no authoritative statement of broad educational goals for the accounting profession officially supported by both the practicing and academic branches of the profession.

The Commission on Standards

In 1949, Donald P. Perry became chairman of the Institute's Board of Examiners. Mr. Perry was a partner of Lybrand, Ross Bros. & Montgomery in the Boston office of the firm. He was thoughtful and studious, but at the same time a man of action. In his work with the Board he noted with concern the small percentage of candidates who passed the CPA examinations. He became convinced that it was inadequate preparation, both through formal education and practical experience, that was responsible for these unsatisfactory results.

In 1951 Mr. Perry delivered an address at the annual meeting of the Institute in which he described the great variety among the states in preliminary requirements for the CPA certificate.

He pointed to the lack of a national standard of education and experience which would encourage the states to move toward uniform requirements. He proposed that a commission be created, composed of representatives of all interested groups, to formulate standards of education and experience for the immediate future, but also "to see that standards are changed with changing conditions, and raised as rapidly as will meet with general acceptance."

Two years before Mr. Perry's speech, the Institute's committee on state legislation had undertaken to revise the model

accountancy law, including education and experience requirements. At about the same time the Association of CPA Examiners had appointed a committee to study education and experience as prerequisites for the CPA examination. In 1951 the New York State Department of Education initiated a study of the CPA law of that state, including consideration of the same subject. The views expressed in the course of these activities on the relation of education and experience were so diverse that the lack of any consensus in the profession became apparent. An independent commission, consisting of representatives of all interested groups, seemed a logical mechanism through which an attempt to hammer out a policy might be made.

The Institute acted promptly on Mr. Perry's suggestion and, in co-operation with the other interested groups, created an independent Commission on Standards of Education and Experience for Certified Public Accountants. Donald Perry was named chairman. Robert L. Kane, Jr., was appointed secretary. He was educational director of the Institute—a full-time member of its staff—and a former professor of accounting. The 24 members of the Commission included practicing accountants from both large and small firms in various parts of the country, a liberal representation of accounting professors and deans of schools of business, not all of whom were accountants, and one educational administrator who had served as associate commissioner of education for New York State. In the first phase of the work, the study director was Professor Leslie J. Buchan, then of the Washington University, St. Louis. In the second phase of the study, Professor Frank P. Smith served in this capacity, with the assistance of Professor Samuel R. Hepworth, both of the University of Michigan.

Financial support for the Commission's study was provided by contributions from the American Institute, 32 state societies of certified public accountants, the American Accounting Association, and ten state boards of accountancy.

The Commission's report was published in 1956 by the Bureau of Business Research, University of Michigan. Fifty-

five thousand copies were distributed over the next few years.

While there was debate and disagreement over the Commission's recommendations, its report nevertheless had tremendous impact on the thinking of all persons concerned with standards for the CPA certificate. It isolated the issues and focused attention on the differing points of view. It also provided foundation materials for later efforts in the same field.

An introduction to the report provided historical background. The text then discussed the professional practice of certified public accountants, the legal regulation of public accounting, the educational facilities for certified public accountants, the experience requirements, and the CPA examination. Recommendations for the future were then presented.

Of major importance, as it later proved, was an introductory statement outlining the following characteristics of a profession, on which there was general agreement:

1. A body of specialized knowledge.
2. A recognized formal educational process for acquiring the requisite specialized knowledge.
3. A standard of professional qualifications governing admission to the profession.
4. A standard of conduct governing the relationships of the practitioner with clients, colleagues, and the public.
5. Recognition of status.
6. An acceptance of the social responsibility inherent in an occupation endowed with public interest.
7. An organization devoted to the advancement of the social obligations of the group.

The report stated that the old and established professions of law, medicine, and theology met these criteria most completely. The CPA profession, it said, met these criteria in varying degrees.

The Commission concluded that the interstate operations of industry and the nationwide application of federal government regulations had eliminated any need that may have

existed for differing standards among CPA jurisdictions. Uniformity of requirements was strongly advocated.

Pointing out that in most professions in the United States the method of qualification had been first through experience only, later through a combination of experience and formal educational training, and eventually through formal education alone, the majority of the Commission concluded that the formal educational process was the more important type of preparation for the practice of public accounting under modern conditions.

The Commission recommended additional academic study beyond the level of the bachelor's degree. It envisaged professional accounting programs, within the framework of the university schools of business administration, which would be comparable in approach and objectives to the professional schools established in other fields.

The Commission recommended that candidates be admitted to the CPA examination at the conclusion of the formal educational process. It was reasoned that experience too often was measured in terms of elapsed time, without regard to variety, relevancy and depth, and that the difficulty of testing and evaluating experience was formidable.

Looking to the future, the majority of the Commission proposed that the formal educational process could be made so effective that it would constitute the principal method of preparation for a career in public accounting. It was suggested that the preliminary requirement for the CPA certificate eventually be satisfactory completion of the educational process; that the experience requirement gradually be eliminated; and that the CPA certificate be regarded as a mark of competence to *enter* the profession—rather than as a mark of competence to practice as a principal. In support of this conclusion, the Commission's report pointed out that in the great majority of states admission to the bar was based on satisfaction of educational prerequisites, acceptable personal qualifications, and successful completion of the bar examinations.

With regard to the ultimate educational process, the Com-

mission recommended that the curriculum for the four-year undergraduate program be based on the recommendations of the standards-rating committee of the American Accounting Association and the requirements of the American Association of Collegiate Schools of Business. The AAA standards provided roughly an equal division of time between cultural subjects and professional studies. Students who had completed the four-year course would be subjected to a qualifying examination for admission to the professional programs in graduate schools of business.

No specific curriculum was recommended, but it was suggested in general terms that the subject matter should cover oral and written communication, auditing, taxes, accounting systems and controls, standards of professional conduct, administration of a public accounting practice, accounting principles, and business policy. (No reference was made to the management sciences or to the computer.)

Tentatively, it was suggested that accreditation of the professional academic program should be undertaken by a new organization, independent of any accounting organizations, but reflecting the viewpoints of both educators and practitioners.

Internship programs of three months, to be included in the professional program, were also recommended.

Finally, it was proposed that individuals be admitted to the CPA examination upon completion of the recommended educational preparation and, if successful, be awarded the certificate.

As a transitional goal, the Commission recommended college graduation, including an accounting major, completion of the uniform CPA examination, and a minimum of two years practical experience in public accounting under the guidance of a CPA.

Four members of the Commission dissented violently, mainly in opposition to the proposals that the CPA certificate be regarded as evidence of qualification to *enter* the profession, rather than to practice it, and that the experience requirement be eliminated ultimately.

The Bailey Committee Report

Since the Commission on Standards was an independent body, its conclusions were binding on neither the Institute nor any of the other organizations which had supported the study. It seemed desirable, therefore, for the Institute to determine the extent to which it would adopt the conclusions as official policy of the national organization of certified public accountants. George D. Bailey was appointed chairman of a special committee for this purpose, which became known generally as the "Bailey committee." Mr. Bailey has been mentioned earlier as chairman of the committee on accounting procedure, and as president of the Institute.

This committee worked for nearly three years. It made a comprehensive study of the Commission's report, conducted an opinion survey of a cross-section of the profession, and consulted officials of all prominent national accounting organizations, as well as interested government officers. Thus expressions of opinions were obtained from practitioners in small, medium, and large firms, in communities of all sizes throughout the country, from accounting professors and deans, and from corporate controllers.

The attitudes of many practicing certified public accountants were in sympathy with the four dissenters to the Commission's report. To them it seemed to downgrade the CPA certificate to suggest that it was only a ticket of admission to the profession, rather than evidence of competence to practice. The idea that practical experience was an essential prerequisite for the CPA certificate was also deeply ingrained. Many practitioners could not accept the proposition that a formal educational process should constitute the only method of training prior to the CPA examination.

These views were emphatically expressed to the Bailey committee, and were reflected in its recommendations, which, in summary, were as follows:

- That the long-established meaning of the CPA certificate

as evidence of demonstrated competence for the practice of public accounting be continued;

- That a bachelor's degree be made a requirement for the CPA certificate, and that the curriculum recommended by the American Accounting Association's standards-rating committee was desirable;
- That no qualifying examination be recommended for the time being to screen applicants for post-graduate education;
- That post-graduate education was desirable and that, as soon as possible, post-graduate study devoted principally to accountancy and business administration should become a requirement for the CPA certificate;
- That no new organization to accredit educational programs be formed, but that an advisory committee of the Institute co-operate with the AAA and the AACSB to assist interested schools in planning and revising courses and programs;
- That student internship as part of the educational process be optional;
- That an experience requirement be retained: with a baccalaureate degree the experience should be not less than two years and with post-graduate education not less than one year; that the experience should be under the guidance of a CPA, and some of it should be in the area of third-party reliance (auditing);
- That the Institute should define acceptable experience for the CPA certificate. (This was designed to meet the Commission's criticism that evaluation of experience was too difficult.)
- That the existing purposes and level of the CPA examination be continued, not to test the results of academic preparation, but to measure technical competence and skill in the application of knowledge and the exercise of judgment. (It was noted that the existing level of the examination, which should be continued, was such as to test competence to conduct a medium-sized engagement, or general practice in a medium-sized community.)

- That a candidate be permitted to take the examination when he felt adequately prepared, but not before he had completed the educational requirements. (This was consistent with the Commission's views.)
- That the certificate be awarded after the candidate had passed the examination and completed the experience requirements;
- That the Institute co-operate with colleges by providing instructional materials drawn from practice, by providing scholarships, internships and funds for advanced study by faculty members, by endowing professional chairs, by providing work experience for faculty members, and by providing special lecturers;
- That the Institute's committee on personnel testing ascertain whether its present testing program could be adapted, or new tests could be developed, to screen applicants for post-graduate educational programs in accounting;
- That proposed legislation to carry out these recommendations be timed with a view to local conditions;
- That the Institute take the leadership in causing periodic reviews of education and experience for CPAs.

This report was presented to the Council in April 1959, and was enthusiastically approved—with a few dissents. For the most part, the recommendations were consistent with the recommendations of the Commission on Standards, but on two vital points the Bailey committee and the Council adhered to the view of the four dissenters on the Commission: that the CPA certificate not be considered as merely a ticket of admission to the profession and that an experience requirement should be retained.

Despite these differences, the action of the Institute's Council in approving the Bailey committee report strongly encouraged professional accounting programs at the graduate level, within the framework of schools of business administration, and the requirement of at least a baccalaureate degree for admission to the CPA examination.

The Hansen Committee Report

There remained the uncompleted task of describing the nature of acceptable experience.

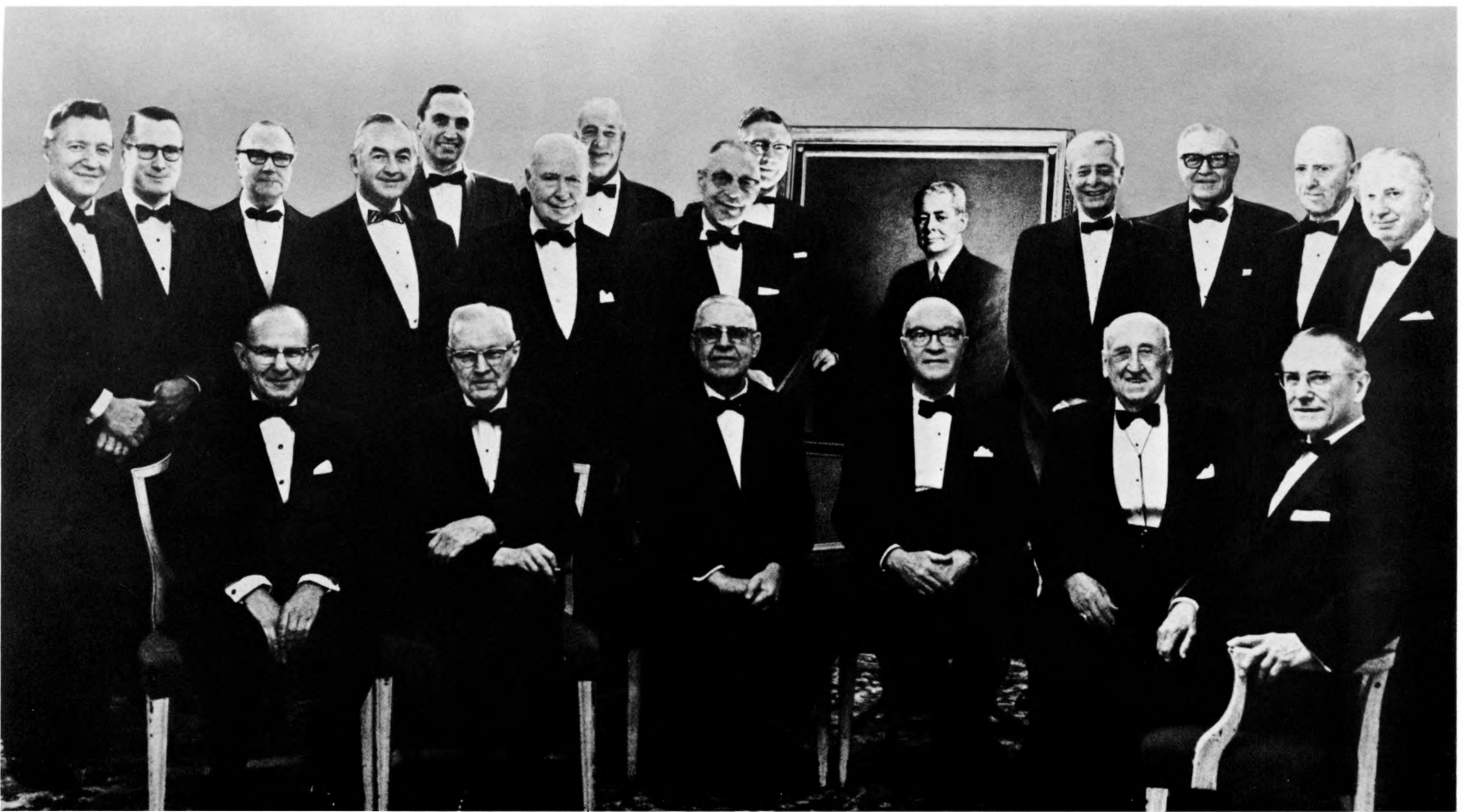
In accordance with the Bailey committee's recommendation, another special committee was appointed for this purpose. The chairman was George H. Hansen, who had become a senior partner of the midwestern regional firm of McGladrey, Hansen & Dunn. Five of the other members represented a cross-section of the profession and the academic world. The seventh member was Joseph Campbell, a member of the Institute and then Comptroller General of the United States.

The Hansen committee, of course, was bound by the Council's decision that the CPA certificate was a mark of competence to practice.

The Hansen committee assumed that the audit function, involving third-party reliance (strongly emphasized in the Bailey report), was a basic activity of the CPA and that the public interest in that activity was the principal reason for licensing CPAs. The committee also assumed that conducting an examination and reporting in accordance with generally accepted auditing standards were the distinguishing features of auditing.

The Hansen committee, therefore, recommended that a minimum of one year of experience should be in public accounting, under the supervision of a CPA (in certain cases under the supervision of a licensed public accountant), and that the experience should include examination of financial statements of diversified businesses, conducted in accordance with generally accepted auditing standards. In cases where experience beyond the one-year minimum was required, the committee recommended that it might be obtained in activities comparable to those of public accounting (presumably in the employ of government or corporations).

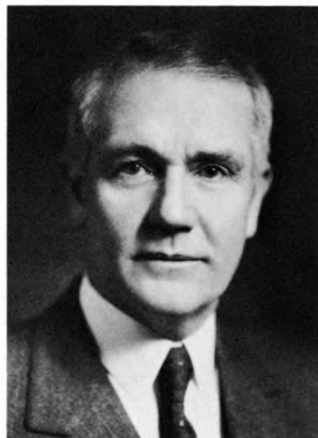
After discussion at a meeting in April 1961, the Council released the committee's report for the information of mem-



Past presidents of the Institute gather to honor John L. Carey on his retirement in May 1969 as executive vice president. Standing (l. to r.), Thomas D. Flynn (1964-65), Ralph E. Kent (1968-69), Hilliard R. Giffen (1966-67), Maurice H. Stans (1954-55), Marvin L. Stone (1967-68), J. Harold Stewart (1949-50), John H. Zebley, Jr. (1955-56), Louis H. Penney (1958-59), Clifford V. Heimbucher (1963-64), John L. Carey, T. Coleman Andrews (1950-51), Arthur B. Foye (1953-54), John W. Queenan (1961-62). Seated (l. to r.), J. S. Seidman (1959-60), Edward B. Wilcox (1946-47), Norman L. McLaren (1941-42), Samuel J. Broad (1944-45), Arthur C. Upleger (1928-29), Louis H. Pilie (1960-61).

Clem W. Collins (1937-39)

John K. Mathieson (1939-40)


C. Oliver Wellington (1940-41)

George S. Olive (1942-43)

T. Dwight Williams (1945-46)

J. William Hope (1951-52)

Marquis G. Eaton (1956-57)

Alvin R. Jennings (1957-58)

Robert E. Witschey (1962-63)

Robert M. Trueblood (1965-66)

Louis M. Kessler (1969-70)

American Institute of Accountants' speakers party, 1944 Wartime Accounting Conferences. Standing (l. to r.), the author, John L. Carey, Victor H. Stempf (1943-44), J. A. Phillips (1952-53). Seated (l. to r.), George D. Bailey (1947-48), George P. Ellis (1933-34), Samuel J. Broad (1944-45).

Two former presidents of the Institute meet with President Eisenhower in January 1958 at Gettysburg, Pennsylvania, to discuss the 1959 budget. With the President are (l. to r.) Percival F. Brundage (1948-49), then Director of the Budget; Dr. James Killian, a special assistant; and Maurice H. Stans (1954-55), Director of the Budget from 1958 to 1961.

Carman G. Blough, the first chief accountant for the Securities and Exchange Commission, retires as Institute director of research in the spring of 1961. J. S. Seidman (left), former AICPA president (1959-60), presents him with an album of letters from friends.

bers of state boards of accountancy, and state societies and their legislative committees. Comments were invited. The report was not adopted as formal Institute policy, since it was recognized that flexibility might be desirable in the light of rapidly changing conditions.

While the Hansen committee report was in process, another event had occurred which had shaken both the practicing and academic branches of the profession.

The Ford and Carnegie Reports

In 1959 two reports were published almost simultaneously, financed by the Ford Foundation and the Carnegie Corporation, and known respectively as the Gordon-Howell and Pierson reports.

Both reports were addressed to current standards of business education. Both sharply criticized the undergraduate business schools for low standards of admission and unsatisfactory teaching methods. Accounting courses received more favorable comment than others, but accounting curricula did not escape challenge. Many accounting courses were said to contain too much descriptive material of a vocational-training type, and too little of the type of instruction that would encourage an individual's maximum intellectual growth. Financial accounting and auditing were regarded as inferior to managerial accounting as subjects for academic study.

These reports stimulated re-examination of business-administration programs in colleges and universities throughout the country. Some undergraduate business schools were eliminated, on the ground that the four undergraduate years should be devoted to liberal arts and sciences and that training in business should be undertaken at the graduate level. Other undergraduate schools tried to adapt their programs to the patterns recommended in the Ford and Carnegie studies by reducing

the "vocational-type" courses and devoting more time to liberal arts and science.

In some schools, at both the graduate and undergraduate levels, emphasis shifted to managerial accounting as contrasted with financial accounting and auditing.

These trends raised serious questions for the accounting profession. Increasing reliance was being placed on colleges and universities to provide recruits for the profession. It seeemed possible, if not probable, that college graduates would have had little more than a broad introduction to accounting principles and auditing standards, to say nothing of tax accounting, before employment by an accounting firm. This would impose a heavy burden of staff training on the firms themselves—a burden which might prove unbearable for smaller firms. Furthermore, the trend might discourage students from seeking employment in the profession or aspiring to become CPAs, since they would have had little exposure to the subject matter related to the principal functions of public accounting firms.

Many accounting teachers were also deeply concerned. Their traditional approach emphasized financial accounting and auditing. Now these subjects might be downgraded, on the assumption that they were of a "descriptive" or "vocational-training" nature.

In view of the Ford and Carnegie reports, the Institute's committee on relations with universities conducted five seminars on the future of accounting education, in which invited participants were drawn from public accounting, education, business, and government. The object was to stimulate thought and recommendations. Summaries of the discussions and conclusions at these seminars were published for general information, and were useful to those who later conducted intensive research in this field.

While these problems were being mulled over, a significant suggestion was made by Charles P. Rockwood, then director of public relations for the Institute: that it was time to describe the "common body of knowledge" of CPAs, in terms

that would permit objective evaluation by university authorities and others.

"A body of specialized knowledge" had been the first of the characteristics of a profession enumerated by the Commission on Standards of Education and Experience in 1956. Yet the Commission had implicitly conceded that the body of knowledge that all CPAs should possess had not been precisely described. The Commission had said that there was a common core of accounting knowledge that all CPAs must possess, but that the principles and procedures applicable to some of the required areas of knowledge were not as fully developed, or as exhaustively documented, as those of the older professions.

It was perceived that Mr. Rockwood's insight revealed a need. It seemed highly desirable to describe the "common body of knowledge" of the accounting profession in terms that would permit a fair evaluation by influential individuals not familiar with the profession's activities. To many of these it was possible that "accounting" seemed synonymous with double-entry bookkeeping, auditing seemed to be a detailed clerical task, and financial statements seemed merely summaries routinely drawn from bookkeeping records. Where such misconceptions prevailed, it might be natural to assume that accounting instruction was not of sufficiently high intellectual quality to justify a place on the campus of an institution which prided itself on scholarship.

In 1962 the Institute's committee on long-range objectives (see Chapter 18) recommended, and Council adopted, the following statement:

> It is an objective of the Institute:
>
> 1. To encourage the description and continuous restating of those areas of knowledge and technical competence required by the CPA in his present and prospective professional practice; and
> 2. To bring about the clarification of the areas of responsibility of universities, practitioners and professional societies in the education and training of CPAs.

This was almost a directive for a study of the common body of knowledge for CPAs.

Steps were promptly taken to initiate such a study. Clifford V. Heimbucher of San Francisco, who was then a member of the Institute's executive committee, happened to be personally acquainted with John Gardner, then president of the Carnegie Corporation, which had financed one of the studies containing critical comments about business education in general, and accounting education in particular. Mr. Heimbucher approached Mr. Gardner with a request that the Carnegie Corporation finance a study jointly with the Institute to guide educational institutions in deciding what kinds of accounting courses might appropriately be taught in the business schools. After conferences with Institute officials, who submitted a detailed prospectus, the Carnegie Corporation granted $50,000, with the understanding that the Institute would appropriate an identical sum, to finance the proposed study.

The Institute's Council approved the project, and a new commission was organized to supervise the study. Dean Robert H. Roy, of the School of Engineering Science of Johns Hopkins University, was engaged as study director, and James H. MacNeill, CPA, later Dean of the School of Business of Fordham University, was engaged as assistant director.

Horizons for a Profession

The 12-man Commission on the Common Body of Knowledge for CPAs, appointed in 1963 to supervise the study, was headed by Elmer G. Beamer, partner of Haskins & Sells in Cleveland, Ohio, who had served as a member of the Commission on Standards. The other members included two partners of national accounting firms; two partners of medium-sized accounting firms, one in the west and one in the east; a non-accounting dean of a prestigious graduate school of business; a dean of a college of liberal arts; two widely-known and respected professors of accounting, one in a graduate

school of business, the other in an undergraduate school; a vice president of the New York Stock Exchange; a senior vice president of a middle-western bank; and a partner of an outstanding law firm in Pennsylvania. Edward S. Lynn, who had become the Institute's full-time director of education, formerly a professor of accounting at the University of Wisconsin, served as secretary of the Commission.

The study, which occupied nearly five years, was one of the most extensive ever undertaken on any aspect of the accounting profession. After a review of all related literature, the study director and his assistant developed an elaborate questionnaire, which was widely circulated among accounting firms to determine the current and probable future scope of practice. Catalogs of representative educational institutions were reviewed to determine the nature and scope of accounting courses then being offered. The views of large numbers of individual CPAs were obtained as to the subject matter considered of greatest importance to students who aspired to success in public accounting.

These efforts were supplemented by numerous personal interviews with CPAs in firms of all sizes and in all parts of the country. Many group discussions were also held in conjunction with state society and Institute meetings, at which tentative propositions and questions were discussed by members of the audience.

Frequent meetings of the Commission were held to review the work of the study directors and to discuss their tentative conclusions.

The results were published by the Institute in 1967, in a 354-page bound book entitled *Horizons for a Profession,* with a subtitle, "The Common Body of Knowledge for Certified Public Accountants."

Copies of the book were sent to deans of institutions which were members of the American Association of Collegiate Schools of Business, and copies were purchased by thousands of accounting professors and practitioners.

Horizons for a Profession made a tremendous impression. The principal author was Dean Roy, and the quality of the writing

was distinguished. The logic was tight. The factual bases for the recommendations were sound.

Broadly, the common body of knowledge for beginning CPAs was described as that which at the outset would enable the individual to provide the public with accounting service of at least the minimum necessary scope and quality, and at the same time would equip him with the knowledge and intellectual habits essential to keep pace with the requirements of the changing environment.

The areas of study recommended were accounting, the humanities, economics, behavioral science, law, mathematics, statistics, probability, and the functional fields of business.

Each of these areas was described at length, and was justified in relation to the current and predictable activities of CPAs. High on the list in the humanities was skill in communication by means of written and oral English.

The recommended scope of study in accounting was aimed at a thorough knowledge of the functions of accounting, how its products were utilized, and its part in decision-making processes; an understanding of the nature of the various taxes and their significant characteristics; a good knowledge of accounting theory and of generally accepted accounting principles; an understanding of auditing as a body of ideas which would enable an auditor to create his own audit programs as the need arose. Application of accounting concepts and a general understanding of methods and techniques available, including a basic knowledge of computers and their uses, were included in the accounting field.

Under the humanities, in addition to communications, came an understanding of logic and ethics. Both micro-and macro-economics were recommended. Under behavioral sciences the goals suggested were an understanding of formal organizations and the fundamentals of psychology and sociology, with particular reference to management and motivation of people.

The recommended scope of study in law focused generally on business law.

Mathematics, and particularly statistics and probability theory, were recommended because of the increasing emphasis on management services and the sampling procedures in auditing. Since clients more and more relied on mathematical techniques as a basis for decision-making, it was considered essential that CPAs understand these techniques. In addition, the mathematical procedures involved in information and control systems were considered an essential part of the CPA's equipment.

Under the functional fields of business, it was recommended that the beginning CPA have a satisfactory understanding of finance, production, marketing, personnel relations, and business management.

Each of these general recommendations was supported by detailed analysis.

The scope of subject matter recommended was much broader than that suggested in the report of the Commission on Standards only 11 years before. The contrast was dramatic evidence of the rapid changes in the environment which had occurred in a decade.

The general tone of *Horizons* was sympathetic to the "new look" in business education. Descriptive-type, vocational-training courses in the various areas of subject matter were not recommended; rather stress was laid on basic understanding of principles, and a sufficient general knowledge of techniques and procedures to permit a beginning CPA to adapt to changing needs, and to equip himself by continuing study for specialization.

Even before publication of *Horizons for a Profession,* a committee of the American Accounting Association had come to a similar point of view. In its report, issued in 1963, the committee on educational standards said, "The subject matter of accounting encompasses a body of knowledge that lies behind the information system underlying all economic activity. With the advent of high-speed data-processing equipment, it is now economically possible to compile data and make quantitative analyses that were not formerly feasible." These de-

velopments, it was said, had broadened the scope of the accounting function and widened the horizon of the accountant's usefulness in compiling, interpreting, and using quantitative information as a basis for business decisions both within and outside the organization. Well-educated accountants would remain in great demand in the future. One who prepared for a career in accounting, the report continued, must have a background considerably broader than an understanding of accounting concepts and procedures as then understood.

Policy Changes

In 1965 Dr. Guy W. Trump succeeded Dr. Lynn as the Institute's full-time director of education. Dr. Trump had been dean of the School of Business Administration at Emory University. He participated in the later stages of the development of *Horizons for a Profession.* Immediately after its publication he arranged a series of seminars in various parts of the country, in which accounting professors and practitioners joined in discussion of the book. Representatives of 668 universities and colleges participated in these seminars. A summary of the reactions in most cases was referred to the Institute. Broadly, the findings of *Horizons* were approved. As might be expected there were individual reservations about the innovative features of the report, such as the recommended study of mathematics, logic, and behavioral sciences. But generally it was agreed that the book provided useful guidelines for both academic curricula and for continuing-education programs after formal education.

More importantly, the book was considered effective in motivating both educators and practitioners to prepare to meet the continuing challenge of change. Many participants considered *Horizons* potentially as influential as the Ford and Carnegie studies of business education.

The conceptual, as contrasted with the procedural, approach

to formal accounting education was almost universally endorsed in the seminars. The value of general liberal education was not seriously challenged.

It was clear, however, that the accounting firms must expect to share with the colleges and universities the responsibility for the training of accountants. Techniques and procedures, if minimized in the academic curricula, would have to be taught in one way or another by the practicing profession itself.

As in the case of the earlier report of the Commission on Standards of Education and Experience for CPAs, it became necessary for the Institute to decide what policies it should recommend in the light of the evidence and conclusions presented in *Horizons*. The Commission on the Common Body of Knowledge was an independent body, not an arm of the Institute, and it included a number of non-members of the Institute. Furthermore, the Commission had not officially approved the final report, which was presented as the findings of the study directors themselves, as stipulated by the Carnegie Corporation as a condition of its grant toward the financing of the study. This avoided any possibility that the research findings of the study directors might be suppressed or modified by any group swayed by prejudice or self-interest.

The Institute created a new committee on education and experience requirements for CPAs, chaired by Elmer Beamer, who had also headed the Common Body Commission, and including Charles E. Johnson, also a member of the Commission, and James H. MacNeill, assistant study director. Other members of the new committee included practitioners, professors, and one official of the General Accounting Office. This committee was assisted by three members of the staff: Guy Trump, director of education; Robert Schlosser, director of professional development; and William C. Bruschi, director of examinations, the latter serving as secretary of the committee. All three were CPAs and Institute members.

This committee in turn labored for three years. Its first product was a response to the requests of a number of edu-

cators for more specific guidance on curriculum than *Horizons* had provided. After consultation with educators, the committee produced a model program, covering both general education and accounting as broadly defined, with alternative options depending on the intentions of the student. This curriculum followed the outlines of *Horizons* but provided more specific detail. Under general education the subjects specified were communication, behavioral science, economics, elementary accounting, introduction to the computer, mathematics, statistics and probability, and other general courses (embracing 18 to 25 semester hours devoted to study of the humanities, the physical and social sciences or the arts, in order to provide the student with a general exposure). Under general business, additional courses in economics were recommended, as well as courses in the social environment of business, business law, production or operational systems, marketing, finance, organization, group and individual behavior, quantitative applications of business, written communication, and business policy. Under accounting, the specific courses recommended were financial accounting, cost accounting, taxes, auditing, computers, and information systems in business. Adjustments of this curriculum to accommodate a four-year instead of a five-year program were suggested. This material was published by the Institute in 1968 under the title "Academic Preparation for Professional Accounting Careers."

Meanwhile, the "Beamer committee," as it was called, proceeded to discharge its main responsibility which was to recommend Institute policies in the light of the findings in *Horizons*. Again, questionnaires, interviews, and other research devices were employed. Preliminary findings were exposed for comment to a representative cross-section of the profession. The final report was submitted in 1969.

It reviewed studies and Council decisions of earlier years with this comment: "The Institute's present policies are now ten years old and were adopted under conditions existing in the 1950's. Changes in the environment in which entrants to the profession develop their basic professional competence,

changes in the meaning of the CPA designation, and completion of two authoritative Institute studies mark the need for major revisions of these policies." One of the studies cited was *Horizons;* the other was "A Description of the Professional Practice of Certified Public Accountants," prepared by the Institute's planning committee and approved by Council in 1966 (see Chapter 13 and also Chapter 1, Volume I, of this work).

Supported by extensive discussion, factual information and analysis, the report of the Beamer committee recommended the following resolutions:

1. The CPA certificate is evidence of basic competence of professional quality in the discipline of accounting. This basic competence is demonstrated by acquiring the body of knowledge common to the profession and passing the CPA examination.
2. *Horizons for a Profession* is authoritative for the purpose of delineating the common body of knowledge to be possessed by those about to begin their professional careers as CPAs.
3. At least five years of college study are needed to obtain the common body of knowledge for CPAs and should be the education requirement. For those who meet this standard, no qualifying experience should be required.
4. The states should adopt this five-year requirement by 1975. Until it becomes effective, a transitional alternative is four years of college study and one year of qualifying experience.
5. The college study should be in programs comparable to those described in "Academic Preparation for Professional Accounting Careers." The transitional qualifying experience should be in public practice or equivalent experience in industry, government, or college teaching acceptable to state boards of accountancy.
6. Candidates should be encouraged to take the CPA examination as soon as they have fulfilled education requirements and as close to their college graduation dates as possible. For those graduating in June, this may involve taking the May examination on a provisional basis.
7. Student internships are desirable and are encouraged as part of the educational program.
8. The "Report of the Standing Committee on Accounting Education," which provides that the accreditation of academic programs is the responsibility of the academic community, is endorsed. [This

committee, composed of representatives of the American Association of Collegiate Schools of Business, the American Accounting Association, the Association of CPA Examiners, and the Institute, had wrestled with the accreditation problem raised in the report of the former Commission on Standards, and more recently renewed by some academic members of the Association of CPA Examiners.]

9. Educational programs must be flexible and adaptive, and this is best achieved by entrusting their specific content to the academic community; however, the knowledge to be acquired and abilities to be developed through formal education for professional accounting are proper and continuing concerns of the AICPA.

10. The AICPA should review periodically the standards of admission requirements for CPAs.

These proposed resolutions were adopted by the Council at its meeting in May 1969, in spite of strong opposition to elimination of the experience requirement. The Council's action superseded all previous resolutions on the same subject matter.

This latest action was a landmark. After 32 years of intensive study and controversy, a policy had evolved which the academic and practicing branches of the profession could join in approving. Relationships between the two groups had become cordial and co-operative. Both had participated extensively in the evolution of the policy.

To guide the Institute's future efforts in the field of education, the planning committee prepared a program for the profession, which was approved by the executive committee and published in 1968. A long-range plan of action was submitted for implementation by the state societies and the Institute:

1. Pending the requirement of a graduate degree for the CPA certificate, urge those states which have not introduced a baccalaureate requirement to do so.
2. Encourage the widest discussion of *Horizons for a Profession.*
3. Encourage individual members and state societies to improve channels of communication with the academic community.
   (a) Demonstrate concern for the problems of accounting educators.
   (b) Inform educators of practitioners' concern for professional preparation.

4. Encourage and assist in the improvement of faculty.
   (a) Extend the program of financial support to doctoral candidates.
   (b) Urge consideration of teaching as meeting the experience requirements for the CPA certificate.
   (c) Invite faculty members to attend professional development courses as guests of the state societies or the Institute.
   (d) Encourage faculty internships or consulting arrangements with accounting firms.
   (e) Invite selected faculty members to spend their sabbatical leaves working for the Institute.
   (f) Plan and execute summer programs for accounting faculty.
   (g) Study the impact of the profession's financial support for higher education with a view to the possibility of pooling resources.
5. Plan continuing research to expand knowledge of the process of career choice.
6. Expand the professional development programs, both in terms of extension of short courses sufficient to provide a comprehensive curriculum of residence offerings, and in terms of self-study materials.
7. Develop in co-operation with the American Accounting Association and universities a program of "catch-up" education. [The latter recommendation pointed to courses for practitioners who had not acquired some parts of the common body of knowledge, for example, in mathematics.]

All this work had rounded out the claim of certified public accountants to professional status. It reflected the transition begun in 1887 from technician to professional.

Most important, perhaps, it harmonized the profession's need for well-trained recruits with the educational goals of college administrators and faculties. It elevated the teaching of accounting to a scholarly and cultural pursuit, instead of a type of vocational training.

However, it transferred to the practitioners the responsibility of teaching their recruits the techniques and procedures necessary to do their daily work. Fortunately, a mechanism for this purpose was already in existence.

CHAPTER 11

Continuing Education and Recruiting

By the time *Horizons for a Profession* had gained general acceptance, and the Institute's Council had approved the Beamer committee report, there was already in being a successful program of continuing education and staff training. The Institute's professional development program had been established ten years before and had become a successful, self-supporting enterprise.

The need for "catch-up" education for CPAs, and intensive staff training for new recruits to the profession, had become apparent immediately after World War II. The demand for accounting services was mounting. The scope of accounting services was widening. Well-trained manpower was a critical need. By this time almost all new recruits were college graduates, but despite their educational background they needed "how-to-do-it" training. The leisurely approach of on-the-job training of junior staff assistants was no longer economically feasible. The larger firms began to spend substantial sums of money on formal staff-training programs at all levels. The smaller local firms, however, were unable to finance and administer such programs, and their needs became a matter of concern to the Institute.

"Contemporary Accounting"

The first Institute venture into continuing education was the preparation of a refresher course for returning servicemen at the conclusion of World War II. A special committee appointed for this purpose was headed by Raymond E. North, a partner of Haskins & Sells. Among the seven committee members were three future presidents of the Institute—Maurice H. Stans, T. Dwight Williams, and John H. Zebley, Jr. In its first report the committee said:

> The Council and the executive committee recognize that there is an obligation on the national professional society to make the best possible effort to meet the need for retraining members of the profession who are discharged from the armed services after the war. . . . Refresher courses should be of great value to individual veterans in reorienting them to the requirements of the profession, and in reinforcing their self-confidence through familiarizing them with the professional and technical developments since their withdrawal from practice.

Staff assistance was provided by Thomas W. Leland, who served as editor. He was professor of accounting at Texas A & M College and had taken a leave of absence to become the Institute's full-time education director.

Conferences were held with officials of the Veterans Administration and with prominent educators.

It was decided to pitch the course at the level of the semisenior staff accountant, assuming previous education and some experience in accounting. The subject matter to be covered included auditing and reporting, federal and state taxes, and government relations with business. It was proposed that the course would be given on a residential basis on university campuses in principal centers throughout the country.

Under the energetic editorial direction of Professor Leland, the course was completed and published in 1945.

Chapters were written by prominent members of the profession recognized as experts on the topics with which they dealt.

A few of the well-known names appearing among these authors are: Carman G. Blough, William W. Werntz, Thomas H. Sanders, William A. Paton, Eric L. Kohler, Percival F. Brundage, Hiram T. Scovill, Walter A. Staub, George D. Bailey, George O. May, Samuel J. Broad, Maurice E. Peloubet, Maurice H. Stans, C. Oliver Wellington, Mark E. Richardson, J. K. Lasser, Marquis G. Eaton, Eric A. Camman, and John H. Zebley.

The book included 700 pages of printed matter. The first printing of 9,600 copies was immediately exhausted, and a second printing was undertaken. More than 5,000 copies were ordered by public accounting firms and individual accountants —indicating that the book was of value not only to veterans, but as a basis for self-education and staff training by practicing accountants. More than 2,500 individual orders were identified as from returning servicemen, and more than 500 from educational institutions.

The Institute did not undertake to administer any in-residence courses on a national scale, although it encouraged formal courses based on the book to be administered by state societies or by educational institutions. A few state societies sponsored such courses, but mainly the book was used for self-study or training programs within firms.

The success of this project indicated that there was a latent demand for continuing-education materials throughout the profession.

Focus on Staff Training

The Institute's committee on education developed a long-range program in 1944-45, the final item of which was "Problems of staff education as distinct from preparatory education." As a step toward the development of better staff-training programs, the committee offered an honorarium of $500 for the best training program on the art of writing.

Fifty-two papers were entered in the contest, which was

won by Professors George Owen and Richard Gerfen of Northwestern University. The committee then considered the possibility of developing a staff-training manual to be made available to the entire membership of the Institute. Some members of the committee, however, felt strongly that staff-training programs must be tailored to the special needs of each practitioner or firm, and the idea was tabled.

But the vast majority of the smaller local firms had no programs at all, and it gradually became clear that they needed help from the professional societies if they were to offer systematic staff training of any kind.

As mentioned in Chapter 10, the graduate-study conferences, which had taken firm hold in a number of states, had proved most useful to partners of smaller firms and individual practitioners. However, their success led to consideration of more formal methods of instruction. The California Society of Certified Public Accountants was the first to experiment with formal technical courses, prepared with the co-operation of faculty members at the University of California, and administered by practicing CPAs. The Michigan Association of Certified Public Accountants also experimented with course materials suitable for "in-house" administration by local firms.

"The Million-Dollar Handbook"

Meanwhile, two of the most creative minds in the profession had exchanged thoughts about the needs of local firms for information on all phases of the management of a public accounting practice, including staff selection and training. The two men concerned were Maurice Stans, who had been a member of the committee which prepared *Contemporary Accounting,* and Marquis G. Eaton of San Antonio, Texas, head of his own local firm, who had written one of the chapters in that refresher course. They proposed that the Institute provide a

manual on practice management to be called *The CPA Handbook.*

Their project was approved. The committee appointed in 1950 to carry it out was headed by Mr. Stans, and included Mr. Eaton, Arthur B. Foye, senior partner of Haskins & Sells, and Robert E. Witschey, who have been introduced in earlier chapters. All four men were to become presidents of the Institute.

Professor James L. Dohr of Columbia University was appointed editor of the manual, but soon found it necessary to be relieved because of ill health. The Institute's education director, then Robert L. Kane, Jr., assumed the editorship in addition to his other duties.

It was intended that the new manual would not deal extensively with technical subjects, but would focus on how to run a practice. Five hundred small firms and individual practitioners filled out questionnaires relating to their own practices and methods. Thirty substantial local firms agreed to review and check the information secured by these questionnaires.

Twenty-seven chapters were outlined, and authors were selected for each. Consultants from larger firms consented to review the manuscripts of the several chapters.

The CPA Handbook was published in two volumes in 1953. It covered such pragmatic subjects as building and keeping a clientele, partnership agreements, legal responsibility and civil liability, office management and records, staff selection and training, procedures for technical supervision and review of work, fees for services, planning and control of audit procedures, accounting principles and their application, report writing, tax practice, and the CPA as a business consultant.

In view of the wealth of professional talent donated to this production, the manual was dubbed "The Million-Dollar Handbook."

The reception was enthusiastic. More than 10,000 copies were sold immediately. Chapters were utilized in some of the graduate-study conferences. The Mexican Institute of

Certified Public Accountants was granted permission to translate the work into Spanish. Complimentary reviews appeared in accounting publications in England and other countries. One group of chapters was assembled into a paper-bound volume offered for use in colleges and universities.

Again, however, the Institute was not in a position to sponsor formal residence courses based on the contents of the manual.

The First Institute Courses

In the spring of 1952, the chairmen of three committees addressed a joint communication to the Council of the Institute. They were Raymond G. Ankers of Lybrand, Ross Bros. & Montgomery, chairman of the committee on selection of personnel; Thomas D. Flynn of Arthur Young & Company, chairman of the committee on personnel reference; and Louis M. Kessler of Alexander Grant & Company, chairman of the committee on education. They pointed out that these three committees, and to some extent the Board of Examiners of the Institute, had been charged with related responsibilities bearing on the kind and quality of personnel entering the accounting profession. Their communication continued:

> These committees believe that the caliber of the personnel which enters public accounting and decides to remain in public accounting is a matter of vital concern to the profession. . . . At the present time, it is generally recognized that there is a shortage of well-trained and desirable personnel. . . . The chairmen of these committees feel that the problems of recruiting, educating, selecting and subsequently training accounting personnel are of enough importance to warrant a review and reconsideration of the Institute's activities in these areas.

The Institute's present programs, it was said, lacked a coordinated approach to the whole problem. The committee on selection of personnel was concerned solely with adminis-

tration of a testing program. The committee on personnel reference was attempting to provide some placement assistance for students. The committee on education—having extricated itself from arguments about what the schools ought to teach, how they ought to teach it, and how they should be accredited—was concerning itself with internship programs, graduate-study conferences, and possible staff-training plans.

It was recommended that the Council create a major committee to deal with the broad problems of accounting personnel. The three chairmen suggested for that committee a comprehensive outline of activities in the fields of recruiting, aids to education, and continuing-education programs for practitioners and their staffs. On the latter topic, the chairmen said:

> It is believed that the committee can make a substantial contribution through the development of student societies, the development of staff-training programs which can be used by groups of firms or state societies, the development and supplying of material for more advanced study groups, and the possible development of correspondence courses if the need cannot be met in other ways.

In response to this recommendation, the Council authorized consolidation of the activities of all existing committees dealing with accounting personnel in one large "committee on development of accounting personnel"—a title soon after abbreviated to "committee on accounting personnel."

One of its major objectives was improvement of the training and professional development of non-certified junior staff men: "The committee agreed generally as to the desirability of centralizing the preparation of such programs [co-operative staff-training programs] if the state societies wished to establish and operate them. The Institute could aid in the preparation of course material and the interchange of ideas. It was decided to canvass the state societies as to their interest in such a project before any expenditures are made for the production of course materials."

A questionnaire to state societies revealed strong interest in

continuing-education programs for members and their staffs.

The Institute committee was fully aware of the difficulty of preparing high-quality courses. Instead of trying to develop a comprehensive training program, it decided to proceed more slowly, starting with a limited number of carefully prepared courses on specific subjects and trying them out on a pilot basis. In order to employ a qualified staff assistant, a budget of $15,000 was requested for the fiscal year 1954-55. The California Society of Certified Public Accountants gave the committee the benefit of the Society's experience with continuing education.

Professor Paul Fertig, of Ohio State University, was engaged on a one-year leave of absence to assist in development of course materials, under the general supervision of Robert Kane, educational director.

The first two subjects selected were administration of a tax practice and report writing. These were to be "live" courses, of the seminar type, attended by participants at six or eight sessions of about two hours each. This pattern was based on the assumption that both participants and the state societies administering the courses would prefer one session a week, in the evening or on Saturday, so as to interfere as little as possible with working time. The first course, on report writing, was given a trial run in the fall of 1954. The material proved useful, but revisions were necessary, and a more extensive instructor's manual was required. Attendance at this course during the spring of 1955 was estimated to be between 150 and 175.

The course on administration of a tax practice was tried out in the fall of 1955. Courses on accountants' liability and the auditing of accounts receivable were in preparation. Professor Fertig, whose year's leave of absence had expired, returned to Ohio State University. In the first year the report-writing course had been given to eight classes in five states. The program was reaching only a small segment of the profession.

The Michigan Asssociation of Certified Public Accountants

urged preparation of materials which could be used within a firm to train its own staff members. Professor Lawrence, of Michigan State University, was engaged for this purpose.

In 1956, the committee reported that the seminar on accountants' legal responsibility had been completed and tested and that "three or four cities" expected to give the course in the fall of that year. In reviewing its work thus far the committee said, "While demand for the courses has not been exceptional, it appears that as more people become familiar with the program there will be increased usage of the materials." In all, 31 classes used one or more of the three existing courses during the fall of 1956.

A Turning Point

In that same fall of 1956, Marquis G. Eaton, who has already been mentioned several times in earlier chapters, was elected president of the Institute. He had a rare capacity for innovation. He read widely and thought deeply. As president he addressed himself to analysis of the profession's problems and consideration of what the Institute could do to help solve them.

His concern was largely with the problems of the local firms and individual practitioners. He saw that the large national and regional accounting firms were led by able and progressive men and had the resources to do for themselves what was needed to adapt to the changing environment. The Institute, he thought, should serve as a catalyst to enable local firms, on a co-operative basis, to do what none of them could afford to do alone.

Mr. Eaton's contributions during his one year in office were impressive. Some of them have already been described. He inspired the headquarters staff to make improvements in the management of the organization itself. He initiated the long-

range planning activity described more fully in Chapter 18 of this book. Informally, he worked hard at improving communications between the large multi-office firms and the local firms. He initiated a program of studies of the economics of accounting practice (later known as the management of an accounting practice), and also the first inquiries into the CPA's responsibilities in tax practice. But one of his major achievements, to be considered in the present context, was reorganizing the Institute's continuing-education program at a new and higher level.

Without doubt there was a vital need. Many local firms were not training their staffs, were not keeping up with new techniques, were not familiar with rising technical standards, and lacked opportunity for consultation on all sorts of problems, technical and administrative, involved in the conduct of their practices. President Eaton felt that the slow pace at which the Institute was developing courses would not satisfy the need fast enough.

The example of the American Management Association, in the conduct of its amazingly successful educational program for business executives at all levels, was challenging. Mr. Eaton concluded that a similar job could be done for the accounting profession, albeit on a more modest scale, if the program were run on a businesslike basis, as the AMA program had been run—with the work being performed by a full-time, well-paid staff under the general supervision of a volunteer committee, and with participants charged fees adequate to cover all costs.

When he submitted his proposal for reorganization of the continuing-education program to the executive committee, however, opposition developed. This was a new and somewhat radical idea. It was asserted that local accounting firms would never pay enough for educational courses to make such a program self-supporting and that it would be unfair to use the dues of the membership as a whole for the benefit of the relatively small number who might participate.

Patient and persistent argument at length overcame these

objections. By the end of his year in office, President Eaton had gained approval of a new approach to continuing education, with a grant of $50,000 to launch the program.

It took a year to organize the new program, but its sponsor was not fated to see the results. In the fall of 1958, the Council reported:

> Last year at New Orleans we applauded the report of the retiring president, Marquis G. Eaton, who had given our profession a year of vigorous and inspiring leadership. Only a few months later he was no longer with us.

Mark Eaton had died of a heart attack while sitting with friends at his country club in San Antonio, but the ideas which he had left behind him survived and flourished.

The Professional Development Program

It was understood that the new educational project would pay its own way and would recover the capital invested in its development. The possibility of ultimately forming an educational corporation controlled by the Institute was recognized. The "Board of Managers" elected to supervise the project was intended to act as a board of directors of a corporation, not participating directly in operations, but controlling policy and finances. The new director was to be given more authority and more responsibility than had usually been associated with staff positions.

The initial appropriation of $50,000 was earmarked to develop and test the new program. The Council was warned that additional amounts might be needed, perhaps as much as $100,000, to launch the project on a wide scale—and this proved to be true.

Louis W. Matusiak was appointed director of professional development in 1959. He had been an associate professor of

accounting at Detroit University and subsequently had served as training director in the Detroit office of Touche, Ross, Bailey & Smart. He was a young man of inexhaustible energy, tremendous drive, and winning personality—a CPA and a member of the Institute, with sound technical background. He recognized in his new position an opportunity to render a professional service of great magnitude.

He inherited the courses that had already been developed. But experience had indicated that spreading courses over a period of weeks, in bites of two or three hours a week, had many disadvantages from an educational point of view. It was decided to offer one-day or two-day seminars, limited to small groups, and planned on sound educational patterns, but dealing with eminently practical subjects. The objective was to increase the "billable competence" of the participants—as Richard Claire, a member of the Board of Managers, put it.

To attract widespread interest in the new program, it was decided that the first seminar would be on the subject of accountants' fees. It was held at the Biltmore Hotel in New York and was an instant success. It spread like wildfire throughout the country, attracting hundreds of participants. This course had a profound impact on the fee structures of local firms and sole practitioners.

The new program, like the old one, envisaged administration of the courses under state society auspices, but it was also provided that if state societies could not conduct the courses, the Institute might administer them in areas where practitioners indicated a demand. Regional courses, on a larger scale, were to be administered directly by the Institute. The first of these, "Building an Accounting Practice," was held in Washington, D.C., over a two-day period. It drew participants from all the nearby states. This, too, was an instant success, and was repeated in various parts of the country.

One of the most ambitious initial projects was development of a junior staff-training program, to occupy a period of two weeks, and to be conducted on the campuses of universities in the several regions of the country. Many of the national

firms co-operated generously in making available to the Institute their own staff-training materials, which had been developed at substantial cost over a period of years. Mr. Matusiak and his staff adapted these materials to the needs of local firms, which were expected to be the most numerous participants in the staff-training program.

At first it was hard to attract enough participants to make the junior staff-training program self-sustaining. Many local firms hesitated to release a newly employed junior accountant for a period of two weeks, and to pay a fee of several hundred dollars for his tuition and living expenses during that period. Spending money on professional development was a new idea to most CPAs.

But after a year or two the idea caught fire, and thereafter the program was an established success. Later, a staff-training program for supervisory personnel was launched successfully.

Meanwhile, seminars for principals and partners were developed on various aspects of financial reporting, auditing, taxes, and management services, including a series on computers. Different types of courses and materials were also tried out, including lecture programs available to larger numbers, regional programs, and self-study programs via programmed learning materials, record discs and tapes.

After five years on the job, having put the program on a self-sustaining basis, and assured of its success, Lou Matusiak resigned to become a partner of Alexander Grant & Company. His place was taken by William Salowe, who had served as assistant director, and under his management the program grew and progressed. However, he too resigned to accept a position with a public accounting firm.

The third director of professional development, Robert Schlosser, had been a professor of accounting at the University of Buffalo. He had also helped conduct the training program of a large accounting firm. Under the guidance of Dr. Guy Trump, educational director of the Institute, Professor Schlosser extended the program even further than before,

enlarging the staff and improving promotional and administrative procedures.

The 1969 catalog included 42 seminars, courses, lecture programs, and training programs, with 17 additional titles currently in preparation. The courses covered both basic and advanced aspects of accounting and auditing, taxation, management services, data processing, and practice management. In addition, programmed learning texts and recorded materials, including a new "CPA audio program," were offered. Total enrollment in the courses in 1969 was estimated at 25,000. The budget of the professional development division was approaching a million dollars.

The Institute's continuing-education activities became a powerful force in maintaining the professional competence of CPAs and their staffs in a period of proliferation of new knowledge. The need was perceived in the 1940's. Ten years of experimentation and small-scale efforts followed. Then a bold new approach was undertaken. Working capital was provided. Competent people were employed on a full-time basis, with authority to do the job that needed to be done, subject to effective supervision and controls. Business methods were employed, and basic principles of management were followed. Modern promotional and marketing methods were employed. Risks were taken and mistakes were made, but the need proved to be real, and the latent demand became effective. Resounding success crowned the effort.

Attracting Competent Personnel

It was perceived, however, that the most elaborate educational facilities were of little value unless the students had the capacity to benefit from the instruction. In the economic boom following World War II, the competition for brains

became savage. Corporations, universities, government agencies, and the professions were bidding for bright college graduates.

The larger accounting firms were the first to see that they would have to compete vigorously if they were to maintain competent staffs. They began systematic recruiting procedures, usually under the direction of partners who spent full time at this task. Attractive brochures were prepared, interviews were conducted at campuses all over the country, and before long a steady procession of high-ranking accounting majors was flowing into the offices of a relatively small number of firms.

Local firms and individual practitioners were at a disadvantage. It was difficult for them to spare the time of principals to conduct personal recruiting efforts. At first it was also difficult for them to pay competitive starting salaries. They hesitated to hire more assistants than the current volume of work required, and thus often found themselves understaffed when confronted with opportunities for growth.

The academic accounting community also was concerned with the competition for brains. Many promising secondary-school students were attracted to engineering, mathematics, the sciences, medicine or the law, in preference to accounting, whose reputation was not as glamorous as that of other professions.

Again, the Institute attempted to cope with the problem, to the extent that its always scarce resources permitted.

The Testing Program

Warren Nissley, as mentioned earlier, had always been deeply interested in the profession's personnel problems. As recounted in Volume I of this work, he conceived and created the Institute's bureau for placements in 1926. This was the first organized recruiting effort attempted by the profes-

sion, which, though highly successful, was terminated by the depression. In 1942, in the midst of the World War, Mr. Nissley became keenly aware of the personnel problems that would face accounting firms when the war ended. He perceived that some corporations were experimenting with "aptitude testing," techniques developed by personnel psychologists to provide indications of individual work aptitudes. These devices had also been used by the military services, with some success, in placing men where they would be most effective.

Mr. Nissley thought that the accounting profession might derive several benefits from similar testing programs. First, the existence of the tests might attract attention of students who otherwise might never think of accounting as a career. If such students scored high in the tests, they might be encouraged to major in accounting, and enter the profession later. Furthermore, if the tests proved to be sound indicators of probable success or failure in accounting, they might help to avoid the "square peg in a round hole" problem—the waste of time and money resulting from employment of people who proved unfit for the type of work involved.

Mr. Nissley consulted an expert in the testing field, Dr. Ben Wood, director of the Educational Records Bureau, an adjunct of Columbia University. The Bureau administered a comprehensive series of tests for elementary and secondary schools, and universities, which provided a common measuring stick by which to judge the academic achievement of their students.

Dr. Wood applauded Mr. Nissley's ideas, and offered to co-operate in the preparation of a battery of tests which might help the accounting profession to identify promising recruits. Since the Institute's resources were not adequate for this purpose, Mr. Nissley decided to seek voluntary contributions. He called a meeting of partners of both national and local firms in New York, at which Dr. Wood, armed with charts and graphs, explained what a testing program might do for the profession. One of his most persuasive points was the demonstrable fact that the level of academic achievement

among colleges and universities varied widely. An A student at one college might not have been able to receive a B grade at a college with a higher standard, and a C student at a top-flight institution might be the equivalent of an A student at a college at the lower end of the scale.

Recruiting efforts aimed at the "top 25 per cent of the class" were therefore meaningless without some indication of the academic standards of the different institutions. Since this information was strictly confidential, the only other way to determine the relative academic abilities of prospective recruits was to give the individuals a uniform test.

There was much skepticism among the accountants about the validity of tests of this nature. However, most of those at the meeting were persuaded that the tests might provide useful, if not conclusive, indications of individual potential in accounting.

As a result, about $80,000 was contributed by firms, and $20,000 by the Institute, to get the project going.

A committee on selection of personnel was appointed, with Mr. Nissley as chairman. Dr. Wood and his associates at the Educational Records Bureau proceeded to develop a battery of tests. This involved both research and experimentation, in the course of which more than a thousand successful accountants submitted to tests as a means of checking their validity. The final result was a series of tests: the first to determine general interest, though not necessarily competence, in accounting; the second to determine native intelligence, but with an orientation toward business and accounting subject matter; and the third to determine "achievement"—that is, knowledge of accounting, at two levels, first at the end of the elementary accounting course in the first year of business school, and, second, at the termination of the college course or "the point of employment." Later, additional tests were devised for high-school students, and for evaluating staff members with a view to promotion.

The next step was to get the tests used. At this point Mr. Nissley yielded the chairmanship of the committee to Harold

R. Caffyn, a partner of Hurdman and Cranstoun, who also had a keen interest in the development of personnel. For some years the Institute subsidized the program, while efforts were made to reach a break-even basis.

The principal users in the beginning were colleges and universities. Their interest was twofold: to judge the competence of freshmen to continue with an accounting major and, later, to receive a confidential report of how their accounting majors compared with those of other institutions.

Gradually, however, accounting firms began to see the advantage of the tests as an indicator of likely success in accounting. If the tests had been given in college, the scores were made available to prospective employers. If not, the tests could be administered by employers as part of the interview procedure.

By 1950 the committee was able to report that 208 colleges had participated in the program, as compared with 159 the year before. The number of tests given exceeded 25,000 as compared with 19,000 in the preceding period. The Dominion Association of Chartered Accountants of Canada had experimented with the tests and had decided to participate in the program. The American Accounting Association had provided active co-operation in encouraging extension of the testing program.

Research revealed that correlation between Institute test scores and CPA examination results was high. Later research indicated significant correlation also between test scores and success in the practice of accounting.

Participation in the program increased steadily among colleges, accounting firms, industrial organizations, and government agencies.

By 1968, 1,270 accounting firms, business corporations, or government agencies had been certified to conduct the testing program in screening new employees or evaluating present staff.

In that year, 14,573 tests were ordered or used by certified entities.

In addition, 301 colleges and universities administered more than 30,000 tests in 1968, and nearly 4,000 high-school orientation test booklets were sold—an increase of 58 per cent over the previous year.

Under the arrangements with the Psychological Corporation, which took over administration of the program in 1965, a portion of the fees received was set aside for research and development.

The program became self-supporting, except for the time contributed by members of the Institute's staff working in collaboration with the administrators.

The objectives of the program were largely fulfilled:

1. To assist colleges in advising students considering a career in accounting.
2. To provide the student and teacher with a progress check early in the accounting curriculum.
3. To assist accounting seniors in finding employment by furnishing objective measurements of aptitude and proficiency to prospective employers.
4. To assist the colleges in comparing the aptitude and achievement of their students with those of a larger group of students.
5. To assist accounting firms in selecting new staff members.
6. To assist accountants in making decisions regarding the retention of temporary employees.
7. To assist accountants in the upgrading and promotion of permanent staff members.
8. To assist in high-school guidance.
9. To assist in the upgrading of college accounting curricula.

Furthermore, the program increased respect for the profession in academic circles since it demonstrated a sincere desire to help the schools and to upgrade the quality of the profession's personnel.

Recruiting Activities

Direct recruiting efforts by the organized profession, as contrasted with those of individual firms, developed slowly over a long period of years.

The Institute's first brochure designed to attract college graduates to accounting, was, as noted earlier, "Accountancy Is a Career for Educated Men," published in 1926. This was not revised until 19 years later, when it was succeeded by another pamphlet, "Public Accounting as a Career."

When all Institute activities related to the attraction, education, and training of accounting personnel were consolidated in 1952 under the committee on accounting personnel, more ambitious recruiting efforts were suggested. Among the proposals were a survey of employment practices of accounting firms, which might be helpful to local firms in improving their personnel policies; a survey of the attitudes of college students and teachers toward the accounting profession; a study of personnel programs undertaken by the medical, legal, and engineering professions; a periodic survey of the employment outlook in accounting; and, somewhat later, what was then a radical proposal, the preparation of a motion-picture film designed to interest high-school and college students in accounting as a career.

In one way or another, either by the Institute or by academic agencies, most of these suggestions were fully or partly implemented over the years.

The proposal to produce a recruiting film evoked lively debate at a meeting of Council in 1953. Some Council members regarded the motion-picture medium as undignified. One prominent member inquired sarcastically whether Marilyn Monroe was to be included in the cast. But more progressive views prevailed. The film was produced by a professional organization, which employed professional actors. The script was written largely by Charles E. Noyes, then the Institute's director of public relations, and later editor of *The Journal*

of Accountancy. An advisory committee co-operated with Mr. Noyes. The title of the film was "Accounting—The Language of Business." It was based on an imagined conversation between a certified public accountant and a friend's son who was considering career opportunities. The film depicted various types of problems encountered by practicing CPAs.

Prints were sold, but were also loaned for showings by educational institutions at the Institute's expense. The film was also offered to local television stations as an educational program. Over the years live showings reached the hundreds of thousands, and television viewers were estimated in the millions.

The ice having been broken, another film was soon produced by the Institute entitled "Helping the Taxpayer." It was intended in part to elicit public support for the CPA's position in tax practice (see Chapter 9). However, since the film depicted the CPA's work in the tax field, it was also used as a recruiting device.

In 1959 another film, "The CPA," showing a day in the life of an individual partner of a local accounting firm, was released for distribution. Over a period of ten years this film was seen by an estimated 20 million viewers, both "live" and via television.

In 1968 arrangements were made with the Canadian Institute of Chartered Accountants to modify its excellent recruiting film, "Men of Account," for American audiences. This color film superseded "The CPA" for general showings.

A more subtle film, "Inc.," not aimed at direct career guidance, but designed as a curriculum aid for use in high-school social-science classes, was also produced and distributed by the Institute in 1968. It showed the role of the corporation in American society, and in so doing showed the role of accounting and the CPA in the activities of the corporation. This film was seen by high-school students in large numbers, and the reactions were overwhelmingly favorable.

A series of brochures on the opportunities in public accounting were also produced. A four-page leaflet entitled

"Professional Help Wanted" was first issued in 1953. Thousands of copies were distributed to high-school and college students throughout the country. Interested students were invited to write for a more comprehensive description of the profession contained in a 24-page booklet entitled "Accounting May Be the Right Field for You."

Efforts were made also to communicate with vocational-guidance counsellors, and the Institute prepared exhibits to be shown at guidance counsellors' conventions.

In 1959 an Accounting Careers Council was formed by five major national accounting organizations—the American Accounting Association, the National Association of Accountants, the Financial Executives Institute, the Institute of Internal Auditors, and the American Institute of Certified Public Accountants. The five organizations believed that efforts to interest students in accounting at the high-school level could be conducted most economically on a co-operative basis, rather than by separate efforts. Once a student had enrolled in accounting courses in college, however, it was agreed that the various organizations would compete for his consideration of the several different career fields within the broad field of accounting.

The Careers Council set up a national center for the distribution of career-guidance materials to high schools throughout the country. Mailings went to mathematics teachers, National Merit Scholarship winners, and others. Posters calling attention to accounting as a career, to be placed on high-school bulletin boards, were also distributed.

After several years the Federal Government Accountants Association and the American Society of Women Accountants were also represented in the Council. Members of the seven sponsoring organizations and their local chapters or affiliated societies were encouraged to supplement the Council's efforts by personal appearances at high-school "career days."

At the college level the Institute undertook an advertising campaign in college newspapers. The ads were carried in approximately 50 college publications in the spring and fall of

1968. Hundreds of favorable responses were received, and as a result the program was continued.

Numerous articles on accounting as a career, prepared by members of the Institute or its staff, were published over the years in magazines and books, including government publications related to career choices.

It seems reasonable to assume that all these recruiting activities had some effect. A study of 1961 college graduates, by the National Opinion Research Center at the University of Chicago, showed that 4.5 per cent of the male graduates throughout the country had selected accounting as a career. Statistics for 1967 showed that 15,692 bachelor's degrees, 1,024 master's degrees, and 43 doctorates were awarded in accounting throughout the United States. The numbers of young people studying accounting were increasing faster than in other professional fields and, relatively, even faster than the entire population was growing.

However, questions about the quality of the accounting profession's recruits began to be raised. A study conducted for the Institute by the Bureau of Applied Social Research at Columbia University showed that a substantial proportion of the college graduates entering accounting were not of as high academic standing and were not as highly motivated toward service as graduates entering other professions.

Other studies indicated that the academic ability of students entering the business schools of the colleges and universities—where most accounting courses were conducted—was slightly below the level of those enrolling in liberal arts and science courses. Also, fewer students headed for accounting careers were National Merit Scholarship finalists or semi-finalists. The inference was inescapable that the accounting profession had not attracted as high a proportion of the most able young people as the older and more widely known professions.

A comprehensive approach toward the profession's recruiting efforts, taking into account both supply and demand and quality considerations, was proposed in 1969. The planning committee, with the assistance of Dr. Guy Trump, the Insti-

tute's educational director, suggested a plan of action.

For the short run, the plan envisaged continuation of the recruiting activities which had proved successful in the past, but with additional efforts to increase the supply of recruits from minority groups, and to intensify communications with accounting educators and vocational-guidance counsellors at all levels.

For the future, the planning committee suggested studies to produce information which would permit development of a coherent long-range plan. Specifically, it suggested that answers to the following questions should be sought:

1. How many new entrants into public accounting will the profession require in the next decade? How many in each year of the decade?
2. What is the turnover experience of the profession by size of firm and by size of office—and the reasons therefor?
3. What kinds of skills and knowledge will be required of the new entrants to the profession—how many with skills in auditing, in taxation, and in management services?
4. What are the personal characteristics, beyond academic achievement, which are required for success in public accounting? Can the relative importance of these be determined?
5. What number of potential entrants to public accounting can reasonably be forecast during the next decade (current enrollment trends and those influences on enrollment which can be identified must be considered in making these projections)?
6. What are the current attitudes of students toward accounting? (A survey should be conducted which will determine what students, both those studying accounting and those who are not, do in fact think accountants are like. This survey should give valuable indications of the appeals which are likely to be effective in recruiting.)

Once the necessary information had been acquired and analyzed, the planning committee recommended development of a continuous, co-ordinated, systematic recruiting effort.

Once left to chance, or trial and error, the attraction of personnel of high quality and the improvement of educational

and training facilities were given a position of high priority among the profession's activities in the second phase of its development.

Within a period of only 20 years, policies and programs were hammered out by the academic and practicing branches of the profession, working together, on questions bearing on the personal competence of future CPAs. The scope of formal education in accounting, the means of supplementing it by staff training and continuing education, methods of screening candidates for the profession, and methods of attracting superior candidates—all these were unsettled problem areas as late as 1950.

By 1969 many had been settled—tentatively. Experience had shown that nothing related to professional competence can ever be settled finally. But foundations had been laid, on which adaptations to changing needs could be fashioned.

CHAPTER 12

CPA Requirements and Legal Regulation

WHILE the profession's efforts to improve the education, recruiting and training of its personnel were moving toward ever higher standards of competence, the legal requirements for the CPA certificate lagged behind. This was inevitable. The ultimate control of standards for admission to the profession had been invested in the state legislatures, which enacted CPA legislation, and in the political authorities who appointed the agencies which administered the laws.

It was also inevitable that pressure to lower these standards, or to create a parallel licensing procedure to give professional status to the non-certified, was forthcoming, since many citizens who wished to become CPAs found it impossible to do so.

Groups of accountants who were unable or unwilling to meet the CPA requirements organized themselves, first locally and later on a national basis, to fight for legal recognition. In the early days their main effort was to obtain CPA certificates

by waiver, and in a few cases they were successful. However, as the certified public accountants grew in number and in prestige this became extremely difficult. The aim of the non-certified accountants shifted to legislation which would create a permanent class of licensed or registered public accountants authorized to do the same things that CPAs were entitled to do, but without having satisfied the legal requirements for the CPA certificate.

The constant threat of adverse legislation made the state societies of certified public accountants hesitant to introduce changes in the CPA laws—including amendments to raise educational standards. Such attempts were likely to evoke amendments introduced by non-certified groups which would have lowered standards.

Educational Requirements

From the enactment of the first CPA law in New York in 1896, to the year 1929, the only educational requirement in any state was graduation from high school. In 1929 New York enacted a law, to become effective in 1938, requiring a bachelor's degree from a four-year college acceptable to the New York authorities, with a major in accounting.

Both the American Accounting Association and the Institute had encouraged such a requirement, and with this precedent they redoubled their efforts. Gradually other states followed New York's example.

By January 1, 1968, 27 of the 54 jurisdictions had enacted laws requiring that candidates for the CPA certificate possess college degrees or the equivalent. Eight other jurisdictions required two years of college or its equivalent, while 19 jurisdictions required only high-school education.

But the actual educational qualifications of candidates were higher than the requirements. In 1966, 88 per cent of those sitting for the examination were college graduates, 5 per cent

had from two to four years of college, and another 2 per cent had attended college for less than two years—leaving 5 per cent of the total number with only a high-school education.

A "college education" for purposes of professional qualification, however, required definition. Where this requirement existed the state boards tended to prescribe the acceptable curricula, sometimes including a specified number of hours in specified subjects, such as accounting theory, auditing, accounting practice, commercial law, cost accounting, economics, and so on.

But it was impossible for the administrative bodies to prescribe the precise content of such courses or to evaluate their quality. Even more difficult was applying their yardsticks to new types of courses introduced at universities with high standards and progressive faculties. At some of the most prestigious graduate business schools, courses were introduced in managerial accounting, quantitative analysis, and similar subjects, which involved accounting and auditing but varied widely from the traditional content of courses in these subjects.

Graduates of distinguished institutions holding masters' degrees were sometimes found deficient in educational background under the rules established in some states, while many CPA candidates holding only bachelors' degrees from other institutions that had literally followed the states' curriculum requirements were admitted to the examinations without difficulty.

The Joint Committee on Accounting Education

The illogic of this situation was so clear that the Institute attempted to persuade state societies, in sponsoring legislation, and the boards administering CPA laws, to adopt a more flexible approach.

To wrestle with this problem a joint committee on account-

ing education was formed, consisting of representatives of the Association of CPA Examiners (now the National Association of State Boards of Accountancy), the American Association of Collegiate Schools of Business, the American Accounting Association, and the American Institute of Certified Public Accountants.

The committee's conclusion was that the curricula standards acceptable to the American Association of Collegiate Schools of Business should be adopted as satisfying the educational requirements of the CPA law. The AACSB was in a sense an accrediting institution. It accepted as members business schools which met standards set by the Association, including standards related to both scope and quality of curriculum. However, the standards relating to scope were flexible, permitting various combinations of courses in accounting and other subject matter.

Whatever combination of courses at undergraduate and graduate levels broadly provided the scope of knowledge outlined in the common body of knowledge study, *Horizons for a Profession,* should be acceptable as meeting educational requirements for the CPA certificate, in the view of the joint committee representing the four organizations primarily concerned.

Experience Requirements

The difficulties which the Institute encountered in developing a policy on the experience requirement have been recited in Chapter 10. Even the enunciation of the policy ultimately adopted was not expected to result in immediate implementation by the states. It was recognized that the change would be gradual, following discussion, persuasion, and acceptance. The Beamer committee was considered optimistic in recommending that by 1975 all states should require five years' education at the college level, and eliminate the experience requirement for those who satisfied the educational standards.

However, experience requirements were "all over the lot." In terms of duration, they ranged from one year to four years, in some cases with credit against experience for specified educational attainments. But the question which led to the most confusion was, What kind of experience? Some states required public accounting experience exclusively, but others accepted equivalent experience in government or industry. Experience in the teaching of accounting was acceptable in some jurisdictions but not in others.

Most baffling was the question of how to appraise the quality of experience, no matter where or how obtained. The mere number of years spent in the employ of a public accounting firm did not reveal whether the time was devoted to write-up work, preparation of tax returns, management services or auditing—or at what level. Several states, therefore, required that a specified proportion of the time must be in auditing leading to the expression of an opinion on financial statements —the area of practice presumed to be most highly charged with public interest.

The trend over the years was away from experience as a criterion of qualification for the CPA certificate—though it survived as a vestigial requirement. By approving the Beamer committee report, described in Chapter 10, the Institute's Council finally called for complete substitution of education for experience as the ultimate goal.

The CPA Examination

With educational and experience requirements ranging from low to high, the Uniform CPA Examination became the only nationwide yardstick by which to measure the technical competence of candidates for the CPA certificate.

The achievement and preservation of uniformity in the written examinations was no easy task.

In 1917, when the Institute first offered a written exami-

nation for the use of state accountancy boards, three states accepted the invitation. At the end of 1937, 20 years later, 44 jurisdictions, including what was then the territory of Hawaii, were participating in what was known as the "plan of co-operation in the conduct of examinations."

Fifteen years later—35 years after the initiation of the plan—all states and territories were using the uniform examination, though it was some years later before all of them also used the Advisory Grading Service. In 1952, when all jurisdictions first participated, there were 20,000 candidates and the Institute was grading over 50,000 subject papers.

In the November 1967 and May 1968 examinations there were some 34,300 candidates, and 125,000 subject papers were graded.

In the beginning the examination took only two days. The subject of accounting, both practice and theory, was given in two parts; the other subjects were auditing and commercial law. A half day was assigned for each paper. In 1942 the Board of Examiners consulted with the Association of CPA Examiners on a proposal to increase the time to two and one-half days, in view of the expanding subject matter which should be covered. Agreement was reached, and in the May 1943 examination five papers were given in three afternoons and two mornings—auditing, commercial law, theory of accounts (now an area in itself), and accounting practice given in two parts. Each paper, again, was assigned a half day.

The relatively low percentage of passing grades throughout the nation was always a matter of concern, and sometimes a target of criticism. But there was wide variation among the states. Those with higher preliminary requirements showed far higher passing percentages than the others. The Board of Examiners reported in 1952 that the passing percentage in the five highest states was double that of the five lowest. Superior college and university instruction in accounting was later demonstrated by research to increase significantly the probability of success.

Many difficulties confronted the hard-working Board of

Examiners in administering a uniform national examination. In the first place, it was necessary to devise questions and problems which would be acceptable to state boards whose candidates had widely varying educational and experience backgrounds. The preparation of questions and problems which would be considered fair by candidates in both industrial and agricultural areas, for example, was not an easy task.

The Board had to guard against being outwitted by the coaching courses which emerged in various parts of the country to assist candidates in preparing for the examinations. The managers of these courses were astute in detecting the likelihood of reappearance of certain types of questions in the examination. The Board tried not to cover similar subject matter in any predictable rhythm.

For many years the members of the Board of Examiners, who served without compensation, did most of the work in preparing the examination. Part-time help was engaged to assist in this process and to conduct the grading. Beginning in the 1940's full-time educational directors were engaged, whose major responsibilities were to prepare examinations well in advance of the date at which they were to be held and to supervise the grading process, all under the direction and supervision of the Board of Examiners.

The grading process presented difficulties. As the volume of papers increased, the work had to be divided among a larger number of graders, and this opened up the possibility of variations in the level of grading. The successive educational directors, all of whom were former college professors, devised control systems which overcame this danger. No grader marked an entire paper, but only one question or problem. The results obtained by different graders on the same question or problem were periodically checked, to determine whether there were significant differences in the percentage of passing grades or failures on that question. If so, conferences were held to reconcile the approaches of the two graders. Later, some questions of the objective type were instituted (the multiple-choice and "true-false" questions), which could be graded by

machine. To this extent the possibility of subjective variations in grading was eliminated.

The necessity for rigid security measures was recognized from the first. Any leaks of the content of a coming examination could have proved fatal to the entire plan. A leak might occur through some member of the Institute's staff, even in the process of typing or multilithing the questions. It could occur at the printing establishment where the questions were printed before distribution to the state boards. It could occur in one way or another after the questions reached state boards in the various parts of the country. The strictest control measures were devised to minimize the risk of leaks through any of these channels.

Until 1948 the Board of Examiners was charged not only with the administration of the examination, but with the duty of screening applicants for admission to the Institute. In that year over 1,700 applications for admission were received. The double duty proved too burdensome, and the Board asked to be relieved of the admissions function. The bylaws were then amended to create a committee on admissions, leaving the Board free to devote its energies entirely to the uniform examination.

The April 1949 report of the Board recognized that a uniform standard of grading was almost as important as the use of uniform questions and problems, but pointed out that the Institute had no authority to compel state boards to accept the grades of its examiners. Efforts were made to have state boards discuss cases in which their findings differed from the Institute's, in the hope that reconciliations would result. As time went on, fewer and fewer differences were reported.

The Board invited the American Accounting Association to appoint a committee to review and criticize both the content of the uniform examination and the grading procedures. An Association committee submitted a report containing many helpful and constructive suggestions. Since that time, the committee has assisted in gathering and submitting questions and problems for inclusion in the examination.

Close co-operative relations were maintained also with the Association of Certified Public Accountant Examiners (now the National Association of State Boards of Accountancy), which met annually in conjunction with the annual meeting of the Institute. At almost all of these meetings representatives of the Institute's Board and the Association exchanged information and suggestions that were related to the uniform examination.

Research was undertaken to assist in judging the validity of the examinations themselves. An analysis was made of the age, education, and experience of candidates taking the examination in May 1949, correlated with their results.

A correlation study was also made of the scores of a group of candidates on both the Institute's orientation tests and on the CPA examination.

Another test of the validity of the examination and the grading was made by comparing the scores on objective-type questions and on essay-type questions of 400 candidates taking the November 1949 examination.

Research of this nature was continued periodically, and any weaknesses in the examinations that were thus disclosed were corrected.

In the years following World War II, the content of the uniform examination appeared to be narrower than the scope of actual accounting practice, which was expanding rapidly at that time. Since the main function of most public accounting firms was the audit of financial statements, the examination questions and problems had been almost exclusively related to auditing and financial reporting. As tax practice and, later, management services assumed greater importance, questions which were derived from these fields were introduced into the examination.

The relationship between the examination and accounting curricula of the colleges and universities also required attention. Some college courses were designed to assist students in passing the CPA examination. Some textbook writers focused on the subject matter emphasized in the examination. State

laws generally specified that the examination should cover accounting theory and practice, auditing, and commercial law. If the content of the examination suddenly varied rather widely from what students had been taught in state universities, for example, objections might have been raised.

Despite all the difficulties and all the limitations, however, the Uniform CPA Examination was highly successful. It was unique among the professions in the United States and was a legitimate source of pride to all CPAs.

The uniform examination established a basic common status among CPAs throughout the nation. Federal government agencies came to regard CPAs of one state as the same as those of another. The uniform examination also facilitated mobility of CPAs in crossing state boundaries.

Along with the development of technical and ethical standards, the improvement in education and training, and the development of high-quality personnel, the uniform examination has been one of the pillars of the professional accounting structure in the United States. As such it has helped to support the increasing responsibility and authority assumed by certified public accountants.[1]

---

[1] Following are the names of the chairmen of the Board of Examiners from 1937 to 1969, to whom a large share of the credit is due for achieving and maintaining complete uniformity in the CPA examination throughout the nation:

Maurice E. Peloubet	1936-1939	Richard H. Grosse	1956-1959
John H. Zebley, Jr.	1939-1942	William H. Holm	1959-1963
Henry E. Mendes	1942-1946	Ernest A. Berg	1963-1964
J. William Hope	1946-1948	Robin Dee Koppenhaver	1964-1965
Donald P. Perry	1948-1951	W. Kenneth Simpson	1965-1966
Herman W. Bevis	1951-1954	Francis M. Linek	1966-1967
Louis M. Kessler	1954-1956	John A. Baker, Jr.	1967-1968

Samuel I. Diamond, Jr. 1968-1969

In recent years, William Bruschi, CPA, director of examinations, has played a key role in the management of the examinations.

Legislative Problems

Since the ultimate control of CPA standards was in the state legislatures, vocal opposition to elevation of the standards was bound to slow down action. Legislators preferred not to take sides in controversies among members of their constituencies. Rather, the protagonists were urged to compromise their differences and agree on a mutually acceptable program.

As noted above, the elevation of CPA standards was actively opposed on many occasions by organized groups of non-certified accountants who aspired to become CPAs and objected to changes which would make this more difficult. As time went on, however, the possibility of their attaining CPA certificates on a wholesale basis became remote, and their efforts shifted to legislation which would license them as "public accountants."

Any effort to strengthen a CPA law, therefore, was likely to be countered either by attacks on existing standards, or by proposals for a *quid pro quo* in the form of separate licensing arrangements which CPAs considered undesirable.

This sort of problem was not peculiar to the accounting profession. The medical profession struggled for decades, not always successfully, against efforts of osteopaths, naturopaths and chiropractors to attain legal status and the right to do some of the things that doctors did. The dental profession had many legislative battles with dental technicians who sought legislative sanctions to "enter the oral cavity." Even the lawyers, though protected by the courts against admission to the Bar of unqualified persons, still had to make strenuous efforts to prevent the unauthorized practice of law by non-lawyers.

To many observers, including some legislators, efforts of the professional "establishments" to maintain high admission standards appeared to be inspired by monopolistic motives—to protect the insiders against competition by keeping the outsiders out. But it would be impossible to keep standards of professional competence at levels acceptable to the public if practitioners who had demonstrated their technical qualifications, and had subjected themselves to rigid professional disci-

pline, were indistinguishable from others who had done neither.

The emerging CPA profession naturally encountered special difficulties in the legislative arena; since its numbers were comparatively small, it had no solid base of public or political support, the relationship of its work to the public welfare was not as obvious as that of medicine and law, and the scope of professional accounting practice had not been authoritatively defined.

These difficulties were compounded by early efforts of some CPAs to restrict the practice of accounting to CPAs alone.

Regulatory Legislation

When CPA legislation was first proposed in New York in 1894, one of the bills submitted would have prohibited practice as a public accountant without a license. Another bill provided for the issuance of a certificate authorizing practice under the title "certified public accountant," but did not restrict public accounting practice to persons who obtained that title. The Regents of the State of New York apparently preferred the second bill, and it was a law of this type which was finally enacted in 1896. Other laws of the same kind, which came to be known as "permissive," as contrasted with "restrictive" laws, were rapidly enacted in other states.

However, not many years went by before some of those who had obtained the CPA certificate felt the need for protection against the competition of unregulated practitioners who assumed the free title of "public accountant"—not readily distinguishable from "certified public accountant."

In 1917, Oklahoma enacted a restrictive law, which seven years later was held unconstitutional on the grounds that it deprived non-certified accountants of their right to earn a living, that it infringed the right of private contract, and that

it tended to create a monopoly for CPAs which was not justified by the public welfare.

In 1924, Maryland overcame some of these objections in a law which confined the practice of public accounting to CPAs and a limited class licensed as public accountants, which consisted of non-certified accountants in practice at the time of passage of the act. This preserved the rights of existing public accountants, but promised ultimate restriction of practice to CPAs when the "dying class" of licensees ceased to exist.

A similar bill passed the legislature of New York in 1924, but was vetoed by Governor Smith on the ground that many young people would be deprived of an opportunity to render useful accounting services by the ultimate restriction of practice to CPAs.

Nevertheless, other state societies succeeded in having similar legislation adopted, including Tennessee in 1925. But seven years later the Tennessee Supreme Court held this law unconstitutional, on the ground that the definition of the scope of public accounting practice restricted to licensed persons was too broad: it included accounting service of any kind to as few as two employers. This, the court held, abridged the right of private contract. However, the court did say that there were specific types of accounting and auditing work which might sufficiently affect the public interest to justify their restriction to licensed persons.

Up to this time the Institute had taken no position on the highly controversial question of "regulatory" legislation, but in the light of the court decisions and other considerations, the Institute's Council resolved in 1934 that the regulatory accountancy laws of the two-class type were inimical to the interests of CPAs and of the business public. This conclusion was based on doubts as to the constitutionality of such laws; on indications that they impeded the interstate practice of accounting; and on the belief that they diluted the prestige of the CPA certificate by extending legal recognition to unaccredited accountants who were in practice at the time the legislation was enacted.

This action placed the Institute in a policy position contrary to that of many state societies.[2]

At that time many state societies were confronted with legislative battles at every session of the legislatures. All sorts of proposals which, in one way or another, would have diluted the prestige of the CPA certificate were fought off at heavy cost, both in terms of money and the time of the profession's leaders. And not all of the attacks were fought off. Every now and then a bill would pass which granted CPA certificates without examination to a special group, or accorded professional status in some form to non-certified accountants.

State legislation was obviously the prerogative of the state societies, but the absence of a nationwide policy was a handicap. Each society made its own policy, and the policies differed widely. No philosophical base for the positions taken by the different CPA organizations had been articulated. While political decisions were rarely made solely on logical grounds, the absence of a persuasive philosophy left legislators in some confusion. The conflicts often degenerated into power struggles, leading to compromises which had no logical justification. A bad precedent in one state could be used as a weapon against the CPAs in other states.

By 1939 nearly half of the state societies were embroiled in battles in the legislatures.

In that same year the New York State Society of Certified Public Accountants, with the advice of legal counsel, and after consultation with Institute representatives, drafted a bill (which was not enacted) that would have restricted to CPAs only that phase of public accounting practice which materially and directly affected the public interest—financial reporting for third parties. The idea was, perhaps, inspired by the Tennessee Supreme Court's obiter dicta some years before, that there might be some areas of accounting practice which could be restricted

[2] The narrative above repeats in brief what has already been written in Volume I of this book; but the repetition seems necessary as background for the recital of subsequent developments.

to licensed persons constitutionally under the public-welfare clause.

In 1940 the Institute's committee on state legislation undertook a comprehensive study of the problems involved in state accountancy legislation, with a view to establishing standards which could be recommended to state societies.

In an effort to extricate the Institute from a position to which many state societies were hostile, and thus enable the Institute to make influential recommendations, the committee said that the question of whether a restrictive or non-restrictive type of law should be enacted was one to be settled in the light of varying local conditions. It therefore recommended that Council withdraw its 1934 resolution flatly opposing two-class regulatory laws. The Council accepted this recommendation and rescinded the earlier resolution, thus leaving the Institute in a neutral position.

The committee on state legislation then turned its attention to questions such as interstate practice, reciprocity, use of the CPA title by firms, the definition of practice, annual registration fees, the experience requirement, the relationship of education to experience, the composition of state boards, the incorporation of ethical rules in accountancy laws, and similar less controversial matters.

In addition, the committee and the Institute's staff did what they could to help the state societies in resisting undesirable legislation.

A New Approach

In 1941 the Institute's committee submitted a number of suggested policy statements for the Council's consideration. A definition of the practice of accounting appropriate for use in a restrictive bill was among them. This definition was consistent with the New York bill: it covered only the auditing or verification of financial transactions, books, accounts, or

records; the preparation of, or the reporting on, financial, accounting and related statements, intended for publication or for the purpose of obtaining credit, or to influence any stockholder or creditor of any corporation, or to influence any person or persons other than those who procured the preparation, certification or verification described.

This recognized that attempts to restrict the practice of public bookkeeping or write-up work, or the preparation of income-tax returns, or general accounting services of interest only to a client would probably not stand up in court. It appeared possible, however, to restrict to licensed persons, and ultimately to CPAs alone, the use of any title including the words "public accountant," and the area of practice involving financial reporting to third parties.

American Bar Association representatives in the National Conference of Lawyers and Certified Public Accountants had indicated approval of regulatory legislation for accountants, saying that they had no quarrel with CPAs, but strongly objected to the actions of many unregulated public accountants (see Chapter 9). Partly because of the lawyers' view, and partly because more and more state societies were advocating regulatory legislation, the executive committee suggested to the Council that it reconsider its neutral position on this highly charged issue. Council responded by a resolution expressing a preference for regulatory legislation, provided that restrictions on interstate practice could be avoided.

This action gave the legislation committee a signal to exercise some constructive leadership. In its 1945 report the committee summarized its position:

> While the CPA certificate has come to have great value in business and financial circles, there has been steady pressure by individuals, who cannot pass the examination but would like to have the certificate, to amend the CPA laws so as to accomplish their desire. Such pressure seems to be growing and spreading. It may be feared that if any substantial number of veterans add their weight to that of fairly numerous existing organizations of non-certified public accountants . . . there will be serious danger of permanently impair-

ing the standard of the CPA certificate, which has been so laboriously built up in the past 50 years.

It seems to be the duty of the American Institute of Accountants, if this danger exists, to take the lead in preparing a co-ordinated and well fortified defense against whatever attacks may be launched.

There are two principal forms of attacks: first, proposed amendment to the CPA law to grant the certificate without examination to special groups (for example, veterans, government employees, and public accountants who have been in practice for a stipulated length of time); second, proposals for new legislation which would provide for the registration of all public accountants and permit them to use a title such as public accountant, licensed public accountant, or registered public accountant, and provide for continued admission for this second class in the future, sometimes by examination, sometimes not. The second form of attack is almost as bad as the first. . . .

In the past 20 years there has been a distinct trend toward regulatory legislation of the two-class type under the sponsorship of the state societies. . . . At present 16 [states] have legislation of this type.

The Council of the Institute, within a period of about ten years, first adopted a resolution in opposition to regulatory legislation, then withdrew it, adopting a position of complete neutrality, and then in 1944 went on record as favoring regulatory legislation provided impediments to interstate practice could be avoided.

The Institute's committee on state legislation, under authority of the Council, has published a form of regulatory public accounting bill which embodies what it believed to be the Institute's present policy on state legislation.

The basic points of this policy were described as follows:

1. Instead of defining public accounting in broad terms, the Institute's form of bill would simply restrict to CPAs and public accountants registered under a "grandfather clause" the use of the titles "certified public accountant" and "public accountant," and the right to certify financial statements. The bill would not prevent anyone, so long as he did not use a prohibited title, from installing systems, keeping books, preparing financial statements without certificate, preparing tax returns, or rendering general accounting services to management alone, in which third parties had no direct interest.

2. The initial registration of non-certified public account-

ants would be strictly limited to persons actually engaged in public practice at the time the law was enacted, since these were the only ones having any constitutional rights. Thereafter no additional non-certified accountants would be admitted to the licensed group.

3. Impediments to interstate and international practice would be eliminated by liberal provisions for the registration of qualified accountants of other states and countries.

4. College training would be encouraged by reducing the experience requirement for college graduates, but the door would not be closed to persons lacking such educational qualifications who were willing to serve a longer apprenticeship.

It appeared that progress was being made toward clarification of the profession's goals, but again internal differences arose.

The National Society of Public Accountants

In 1945 the National Society of Public Accountants was organized by several of the stronger state associations of public accountants. The National Society engaged a full-time executive secretary, embarked on an aggressive membership promotion campaign, and indicated that its principal activity would be advocacy of legislation which would give status to its members.

Representatives of the Institute met with the directors of the National Society at its first annual meeting to explore the possibility of co-operative consideration of problems of mutual interest. The discussion was not fruitful. The National Society aimed at legislation providing for the continued licensing of public accountants, side by side with certified public accountants, with no restriction of the activities of the former, and the reopening of the registration provisions in

the older regulatory states where few, if any, of the non-certified accountants originally licensed remained in practice.

The Institute's legislation committee reported, "Continuous registration, with no time limit to the life of the group of licensed public accountants, would create a perpetual second class of accountants recognized by the state. The distinction between this class and certified public accountants might not be clear to the public as a whole, which might therefore be deprived of the protection inherent in requirements as to education, experience and examination of those who would qualify for professional practice."

Changing Course Again

Partly because of the new threat posed by the formation of the National Society, a resolution was offered at the Institute's Council meeting in May 1947 that the Council reverse its recent approval of regulatory legislation, and instead announce a preference for permissive legislation, and a determination to protect the CPA certificate against attacks.

After several hours of debate this resolution was tabled, but the Council did adopt a resolution abandoning its recent approval of regulatory legislation. Again the Institute was left in a neutral position. In November of the same year, however, Council asked the committee on state legislation to restudy the problem. A full report was submitted in April of 1948.

Referring to the policy developed by the committee itself in the preceding years (qualified approval of regulatory legislation), the report said:

> The ingredients of which this policy is composed have been developed through prolonged and sometimes stormy discussions over a long period of years. A review of the reports of the committee on state legislation for the past ten years in particular will show the reasoning on which the present policy is based. . . .
>
> There has never been unanimity on the subject of regulatory leg-

islation within the profession. There has in recent years been a minority in the Council itself which opposed regulatory legislation. . . . One reason for reconsidering the matter now, therefore, is that the profession as a whole is not yet in agreement. . . .

The long-range objective implicit in the Institute's policy is to protect the public against the practice of public accountancy by persons not qualified.

Various ways of achieving this objective were then discussed, and the report continued:

It cannot be emphasized too strongly that there is no security in any type of legislation nor in any legislative policy. . . . The alternative to the present policy [of the committee] is to disapprove regulatory legislation, or to adopt a wholly neutral position, leaving the matter to the individual states to settle. The second course would appear to be highly undesirable, as it would be simply an avoidance of the responsibility of leadership. It would leave the profession nationally with no objective and no program. A determination to regard the endorsement of regulatory legislation as a mistake, and frankly to reverse the position of the Institute, would give support indefinitely to status quo. This would mean not only taking a defensive position in the face of independent legislation introduced by non-certified groups, but would also appear to approve, even though tacitly, the present situation in which anyone may call himself a public accountant, and in which anyone may certify financial statements without being subjected to professional control or discipline, the public being able to discriminate between unqualified and qualified only to the extent that it recognizes the significance of the one word "certified."

But these arguments did not prevail. The report of the Council in October 1949 said:

The Council this year has maintained the position of neutrality on the subject of regulatory legislation, which was adopted a year ago. . . . There is no doubt the subject remains a controversial one within the ranks of our own profession. The committee on state legislation has submitted a report, from which some members of the committee dissented, in which an effort was made to present a long-range program that would be acceptable to all concerned. These reports are being submitted to the Council for study and will be reconsidered at the

> May 1950 meeting. The Council believes that for the time being each state society must make its own decision on the question of what type of legislation is best adapted to its needs. The Institute will provide information and assistance to the full extent possible to any state society which requests it.

The wind had been taken out of the sails of the legislation committee. Its personnel had changed, and in April 1950 it reported differences of opinion within its own ranks:

> There is general disagreement by this committee with the policy statement in its present form. . . . There is almost unanimity of opinion that the Council should not adopt a policy statement at this time. Inasmuch as the question of legislation will be decided independently by each state society, it seems that the adoption of a policy statement by anything less than a unanimous Council would have little practical effect.

The committee then resumed its efforts to develop statements of principles on the less controversial aspects of state legislation, excluding the taboo subject of regulatory versus permissive legislation.

The state societies went ahead on their own. Regulatory bills in a variety of forms were introduced in an increasing number of states. The National Society of Public Accountants fought skillfully to establish a continuing class of licensed public accountants side by side with CPAs. While most of these attempts were defeated, there were occasional successes which encouraged continued efforts.

The Institute stood in the background, powerless to take any initiative. It supported state societies that desired regulatory legislation and supported state societies that resisted such legislation. Legislative schizophrenia was afflicting the national organization.

Even on less controversial subjects involved in state accountancy laws, the committee on state legislation was unable to reach agreement. Years of effort to develop a statement of policy led to little tangible result. Conceding its own inability

to reconcile conflicting views, the committee reported in 1953:

> Nevertheless, it is apparent that existing state CPA laws are not generally satisfactory. The great diversity in the laws is a weakness in itself; many of them are also seriously deficient with respect to provisions which the Institute has recommended in the past; and finally, some of them are vulnerable to constant attack by other groups.

Since the state societies frequently turned to the Institute for advice, the committee suggested that a series of research bulletins be drafted on the various aspects of accounting legislation, presenting pro and con arguments on each proposal.

By 1954, 27 states, two territories and the District of Columbia had retained permissive CPA laws, while 21 states and two territories had enacted regulatory laws.

By 1955 the first of the research studies sponsored by the legislation committee was issued, on the relatively innocuous subject, "Should state boards of accountancy be composed exclusively of certified public accountants?" The draft of a second study had also been prepared, on the question "Should accountancy acts state categorically that working papers are the property of the certified public accountant?"

The committee's report, however, expressed concern that the Institute's influence on state legislation appeared to be waning; many state societies were neither consulting the Institute, nor informing it of their intentions with respect to legislation.

An Affirmative Policy

In the spring of 1956 the committee on state legislation unanimously recommended that the Institute abandon its policy of neutrality, and go on record as favoring two-class regulatory legislation without continuing registration of public

accountants. The executive committee endorsed this recommendation and asked the Council to adopt it, subject to certain specified reservations.

After another lengthy debate, the Council, by a two-to-one margin, voted to abandon the neutral position.

By the fall of 1956, the legislation committee had presented a model regulatory accountancy bill, reflecting the new policy. Council approved the basic principles involved, while recognizing that details might have to be modified to meet local laws or conditions. Distribution of the committee's model bill was authorized for the information of state societies. Council's report to the membership stated, "The Council believes that the adoption of a uniform national policy on this question will greatly strengthen the profession and hasten the day when public confusion about the qualifications of persons engaged in the practice of public accounting may be dispelled."

In brief, the basic principles underlying the Council's position and the form of regulatory bill were as follows:

1. The public welfare justified the enactment of licensing laws to establish measures of control and standards of competence for professional accountants.
2. Ultimately all professional accounting work should be performed by CPAs who had demonstrated competence by conforming with statutory requirements.
3. Attainment of the ultimate objective in terms of timing and manner of accomplishment must be decided by each state.
4. Constitutional provisions required that public accountants in practice at the time such a law was enacted must be permitted to continue; but by requiring them to register they would become subject to ethical controls and to provisions for revocation of license for unprofessional conduct.
5. No further registration should be permitted except for those who acquired the CPA certificate, since the public would be confused by perpetual licensing of two classes of

professional accountants under similar titles but with different standards.

6. Reopening the registration of public accountants in states which had already adopted a licensing law would be contrary to the public welfare by attributing professional competence to persons who had not demonstrated it.

7. Only CPAs or registered public accountants should be permitted to sign financial statements with any wording indicating that they had expert knowledge of accounting or auditing.

8. No one should be prevented from doing accounting work for more than one employer, provided he did not hold himself out as a CPA or public accountant, or sign financial statements in a manner which added to their credibility.

9. Free passage of CPAs and other licensed public accountants across state lines in response to the needs of their clients should not be impeded by legislation.

In addition, the Council pledged itself to assist and support state societies to the full extent of its ability in upholding the standards of the profession embodied in state legislation.

The Council included representatives of all the states. The report was accepted by the membership. After decades of internal controversy and vacillation the profession's national organization had finally adopted a clear-cut policy.

Negotiations With National Society

However, legislative controversies between the CPAs and the non-certified accountants continued. The battles were costly, time-consuming and of little profit to either group. The possibility was considered of attempting again to establish a co-operative relationship with the public accountants which would minimize the conflicts.

In 1959 the Institute's long-range objectives committee

recommended the following statement, which the Council adopted:

> Pending the time when public practitioners within the accounting function are either CPAs or those with a clearly differentiating title, there will be a group of non-CPAs who are presently permitted to practice as "public accountants" and whose right to continue to do so during their lifetime must be respected. It is an objective of the Institute that CPAs and their professional societies should develop and maintain friendly co-operative relations with this transitional group with the purpose of improving educational, technical and ethical standards and providing aid in fulfilling the requirements for the CPA certificate.

To study means of implementing this objective a new committee on relations with public accountants was appointed. The chairman was Robert E. Witschey, who had been chairman of the advisory committee of local practitioners, a member of the executive committee, and a vice-president of the Institute, and was to become president in 1962. The committee decided that it would be helpful to explore problems of mutual interest with representatives of the National Society of Public Accountants.

The first meetings between the representatives of the two groups were somewhat tense. However, as the meetings continued and the participants became better acquainted, an atmosphere of mutual confidence developed. It was candidly recognized that co-operation between the two national organizations would be impracticable as long as fundamental differences over accounting legislation remained unresolved. It was therefore agreed to try to work out a mutually satisfactory legislative program which could be presented to the governing bodies of both groups.

Over a period of four years the discussions continued. Memoranda were presented by each side for consideration of the other. Gradually agreement on some fundamental propositions was reached.

At each meeting of the Institute's Council the chairman of the Institute's committee on relations with public account-

ants reported what was taking place in the conferences with the National Society's committee. From the start, a minority of the Council opposed any negotiations with that group, but the majority approved the Witschey committee's efforts and encouraged continued negotiations.

By 1963 the two committees, to the amazement of all concerned, had reached agreement on a legislative program. It was designed to achieve clear identification and effective regulation of all those who rendered accounting services to the public. It was hoped that the program, if generally accepted, would eliminate controversy among accountants, and facilitate co-operative efforts to raise the level of all accounting services.

The proposed program provided that accounting services be divided into two categories: the expression of opinions on financial representations resulting from audit, and all other accounting services. It was agreed that ultimately only CPAs would be authorized to perform services in both categories—meanwhile public accountants licensed under grandfather clauses of two-class regulatory legislation would also be permitted to perform them. A new continuing group would be licensed as "accounting practitioners," who would be authorized to perform services only in the second category.

The National Society's committee concurred with the Institute committee in the statement that anyone licensed to conduct audits leading to the expression of a professional opinion on financial statements for third-party use should be required to demonstrate his competence to perform this work; and that the Uniform CPA Examination and other requirements for the CPA certificate were a reasonable test of such competence.

On the other hand, the Institute committee agreed that other accounting services, performed only for the benefit of clients, should also be performed only by persons who were subject to disciplinary controls. The licensing of insurance agents and real-estate brokers was cited as precedent. It was contemplated that the legislation providing for the licensing of "accounting practitioners," authorized to perform all services except the expression of opinions on financial representa-

tions as a result of audit, would be entirely separate from the CPA law of the state. A clear division between certified public accountants and "accounting practitioners" was envisaged—comparable to the division between doctors and nurses, one group authorized to render any and all services in the field, the other limited to a part of it.

When the report of the two committees was published, a number of state societies voiced strong objections. Correspondence ensued among the state societies which resulted in arousing formidable opposition to the proposals.

The governing body of the National Society, however, approved the program in spite of internal opposition. But at its spring meeting in 1963, after spirited debate, the Institute's Council refused to approve it—once more on the grounds that state societies should not be handicapped in dealing with their own legislative problems by official expressions by the national organization which were not acceptable to the societies.

At this Council meeting President Robert E. Witschey was in the chair, presiding over the defeat of proposals which he, as chairman of the committee on relations with public accountants, had worked for three long years to develop.

The National Society, not unnaturally, no longer considered itself bound by the joint report. Co-operative relations were discontinued, and battles at the local level were resumed.

Legislative Conferences

In 1964 the Institute's committee on state legislation, under the chairmanship of William P. Hutchison of Portland, Oregon, inaugurated a series of national conferences on state legislation, attended by officers, staff, legal counsel, and legislative committees of the state societies. These conferences proved useful in improving communication, in identifying common problems, and in exchanging information about the legislative problems and activities of the several states.

Higher Accreditation?

It seemed to some students of the subject that legislative difficulties would retard the elevation of CPA requirements to conform with the rising expectations of the public.

Accordingly, in 1961, the committee on long-range objectives proposed establishment of an Academy of Professional Accounting, which would provide formal recognition of advanced study and superior attainment on the part of members of the Institute (see Chapter 18).

The proposal was based, in part, on studies of the experience of the medical profession, with its College of Physicians and Surgeons, its Academy of General Practice, and its specialty boards, all of which encouraged acquisition of knowledge and skills beyond the requirements of state licensing laws.

This proposal was rejected by the Council at its meeting in May 1962—partly, it was suspected, because it may have seemed to downgrade the CPA certificate.

The history of all professions shows that the struggle to raise standards, and to confine practice to those who have met the standards, is an endless one. Patience, persistence, and eternal vigilance are the price of success.

In retrospect, despite conflict, confusion, hesitancy, and vacillation, the certified public accountants had not done badly, considering their comparatively short life as an organized, identified profession.

But, uniform national standards of competence and uniform national patterns of legal regulation remained far from realization. Progress toward these goals in the years ahead would be essential if the accounting profession was to achieve the full measure of responsibility and authority.

CHAPTER 13

Small Firms and Large Firms

FROM the earliest days of the organized profession, tension existed between the large and the small accounting firms. Usually the tension was latent, but occasionally it flared up in conflict over policies.

The disparity in sizes of accounting firms was much greater than in other professions. Accounting practice encompassed services to corporations, partnerships, and individuals, as well as to non-profit institutions and government units—entities of all kinds and sizes. This naturally resulted in the evolution of accounting firms of all sizes, with wide variations in the nature of their practices.

The structure of the accounting profession, in fact, reflected the structure of the economy of the United States itself. The gap between large and small business had widened significantly by 1960. The giant corporations were said to handle as much as two-thirds of all the business in the country, while millions of smaller businesses carried on the remaining third.

The disparity in size of CPA practice units roughly paralleled

that of business entities. The latest figures available at the time of this writing indicated that there were 14,454 different accounting firms or individual practitioners represented in the Institute's membership. Of this total, 9,287 practice units included 9,287 members—one each. At the other extreme, eight firms included 11,550 members—and one of these alone accounted for just under 2,000.

The remaining 5,159 firms provided 22,023 Institute members. Of these, 2,464 firms included two members each, and 1,103 firms accounted for three members each. Only nine firms, exclusive of the eight largest, had more than 100 AICPA members each; only six others had 50 to 100; only 13 others had 25 to 50. The rest ranged between three and 25.

Institute membership was not a precise measure of firm size, of course, but since the Institute included over 60 per cent of all CPAs, and a much larger percentage of *practicing* CPAs, these figures provided a fairly reliable indication of the wide differences.

These numbers were neither good nor bad—they simply reflected the impact of economic forces on the structure of the accounting profession. They confirmed what was already known to have happened. Many large local firms merged with the national or regional firms after World War II. But at the same time the number of small firms probably more than doubled. With relatively few exceptions, both large and small firms prospered.

However, the nature of their practices, their needs, their attitudes and aspirations were widely divergent.

The largest firms had been established late in the nineteenth century, or early in the twentieth. Some of their clients grew to be among the largest corporations in the world. As these clients expanded their operations across the country, and later across national boundaries, the accounting firms expanded to serve them, establishing offices in principal centers in the United States and in many foreign countries.

Many local firms also prospered and grew impressively in size. However, when clients developed to a point where they

could not be adequately served by a single office, they were sometimes lost to larger firms. In other cases, local accounting firms, in order to hold growing clients, were forced to expand to regional or national scope, or to merge with larger firms.

The rapid growth of the larger firms was also stimulated by expansion of the scope of accounting services—increasingly sophisticated tax services, and special services involving systems, internal controls, and decision-making processes by management.

After World War II the so-called "management services" expanded even more rapidly, moving the larger firms into such new areas as operations research and electronic data processing, which required new knowledge and new expertise. Smaller firms also benefited to some extent, but the national, regional and large local firms, which had the capital and the manpower to train staffs and acquire new skills, were able to exploit new opportunities more rapidly than most local firms.

In addition, as the rules and regulations of the Securities and Exchange Commission became more elaborate, the accounting and auditing work involved in preparing registration statements for new issues of securities required more specialized knowledge. Most of the larger firms assigned partners to concentrate on this area. As a result, investment bankers frequently recommended to companies issuing securities for the first time that they engage one of the larger firms to audit the financial statements to be included in the registration statements for the SEC.

Capital and manpower also enabled the larger firms to conduct extensive recruiting campaigns at the colleges and universities with the result that a large proportion of the most promising accounting majors were attracted to these firms. Many local firms found difficulty in attracting a sufficient number of able young people.

Publicity received by larger firms annoyed some local practitioners. The very appearance of the names of such firms in annual reports of corporations, distributed to millions of stockholders, inevitably added to the firms' prestige. When *Fortune*

and other magazines "discovered" the accounting profession (as will be explained in the next chapter) they focused their interest on the larger firms serving well-known companies.

All these developments aroused apprehension among many small firms.

Mergers

The mergers of small firms with large firms following World War II, and continuing well into the 1950's, were particularly alarming to local practitioners. Some of the oldest and most prestigious local firms throughout the country were absorbed into national firms. It was something of a shock to other local firms to see the biggest local firm in town suddenly assume the name of one of the national firms. Questions began to arise as to whether the accounting profession would follow the course of the automobile industry, with all accounting work ultimately lodged in a small number of giant organizations.

The merger question was thoroughly explored in 1961 by Louis H. Penney, who had served as president of the Institute two years before and headed his own local firm in San Francisco. At the annual meeting he presented a paper based on personal interviews and correspondence with numerous partners in accounting firms, some of which had merged with larger firms. He found that the number of mergers was not nearly as great as was commonly supposed—a total of 163 in the preceding 15 years, though of this number 113 had occurred in the preceding five years.

National firms often sought mergers, Mr. Penney said, to meet the need for new offices in areas where clients' operations were expanding, or to strengthen or enlarge existing offices by acquiring the personnel of local firms. Other reasons were to acquire men of outstanding ability or superior knowledge in a specialized field, to increase personnel sufficiently to support adequate staff-training programs, and to provide volume and variety of practice which would support more partners and

generate greater income in order to attract more able young men.

On the other hand, Mr. Penney found that the initiative for mergers often came from local firms. In many cases their senior partners had passed the age of 60 and were worried about succession. In other cases, perhaps a majority, the desire to retain growing clients was a motive for affiliation with a national firm. Other reasons included the opportunity to secure retirement benefits, difficult for some small firms to provide; a desire to escape from administrative work; and recruiting and training problems which led many younger practitioners to welcome merger with larger firms so that they could devote their full time to areas of practice which interested them. Inability to provide specialized management services desired by important clients was yet another reason why some local firms were interested in merging.

Publication of Mr. Penney's paper in *The Journal of Accountancy,* and resulting discussions of the subject, took some of the mystery out of the merger question and relieved the tension to some extent.

Despite apprehensions about the large firms, all available information indicated that the number of local firms was increasing, that their practices were growing, and that with few exceptions they were continuing to prosper.

Change of Institute's Name

A source of irritation to many local practitioners was the fact that prior to 1957 the American Institute of Accountants did not include in its title the term "Certified Public Accountants." At the time of the merger of the American Society of Certified Public Accountants with the Institute in 1936, an effort was made to change the Institute's name accordingly, but it failed. However, following organization of the National Society of Public Accountants (see Chapter 12) more and

more members were persuaded that the public might be confused as to which organization represented the professionally accredited practicing accountants. As a result, a bylaw amendment to change the Institute's name to American Institute of Certified Public Accountants was adopted in 1957.

Legislative Restrictions

When the regulatory bills requiring a license to engage in the practice of public accounting within a state began to be introduced (see Chapter 12), the opportunity arose, of which some state societies took advantage, to include provisions in the law which would make it difficult for firms outside a state to establish offices within it. Much of the Institute's hesitation in supporting regulatory legislation was due to the fear that it would impede interstate practice. Resolutions of the Institute's Council placed great stress on the need for free passage across state lines. Licensing provisions based on precedents established in law and medicine were obviously inappropriate in a profession whose members had to follow their clients wherever they went.

"In the area of interstate practice the diversity of rules and legal rights and prohibitions reaches an absurdity," said Clifford V. Heimbucher in his paper, "Fifty-three Jurisdictions," which he prepared as a member of the long-range objectives committee in 1961. His article cited artificial barriers to the issuance of CPA certificates to out-of-state CPAs, restrictions which prevented the use of the CPA title by well-known accounting firms, and widely varying provisions for temporary practice by accounting firms from outside the states concerned.

The most widely publicized example of legal barriers against out-of-state firms was the Florida law. In the early days the CPAs of Florida were concerned about the invasion of their state by northern accountants during the winter. These so-called "snowbirds" would combine a holiday in the sun with the

practice of accounting in Florida for three or four months, and then return to their homes in the North. Legal restrictions against these invaders, however, also had the effect of preventing out-of-state firms from establishing offices in Florida, with the exception of two or three national firms which had offices there before the restrictions became effective.

Yet many out-of-state firms—local as well as national—had clients with branches or subsidiary corporations in Florida. Such firms could serve these clients under temporary permits available only for specific engagements, but were not permitted to maintain offices or staffs in Florida. Efforts to establish new offices there resulted in a series of lawsuits over a period of many years, and attempts to amend the Florida accountancy law, which led to conflict and bitterness.

Concerned over the divisive nature of these conflicts—plainly pitting local firms against larger firms—the Institute, in 1965, appointed a committee, headed by Louis H. Penney, to offer the Institute's "good offices" in an effort to find some acceptable compromise solution. While the efforts of this committee were not successful, they may have been indirectly helpful in accelerating a final solution, which was ultimately reached in 1969. Amendments were then made to the Florida law permitting Florida CPAs to practice as partners of out-of-state firms, subject to specific safeguards to protect the standards of the CPA certificate in Florida and to assure legal and professional responsibility on the part of those admitted to practice there.

State Society Relations

Occasionally the tension between large and small firms manifested itself in relationships between the state societies and the Institute. Many of the state societies were largely directed by local practitioners, and the Institute was suspected in some quarters of being dominated by the larger firms. This occa-

sionally led to opposition by state societies to positions proposed by the Institute.

For example, a proposal for "common membership" in the Institute and the state societies—a requirement that to belong to one a CPA must join the other—was defeated largely because of concern on the part of some state societies that it would lead to Institute—and, possibly, large-firm—domination. In fact, the proposal would have preserved the complete independence of the state societies, as well as that of the Institute. But it could have eliminated some duplication of effort, as in the field of ethics and discipline, and would have eventually eliminated the possibility of having one partner join the Institute and another the state society, thereby obtaining the benefits of both at minimal cost.

During its 15 years of competition with the American Society, the Institute had learned the hard way that without the close co-operation of the state societies it could not discharge its own responsibilities adequately. Local implementation of national policies required action at the community level. Maintenance of professional standards required informed leadership in every community. Legislative programs required grass-roots support. Experimentation with chapters of the Institute, side by side with the state societies, had been unsuccessful, as might have been predicted, and proposals to incorporate the state societies as subdivisions of the Institute were likewise futile. Historically, the state societies were independent, and proud of it.

Following the merger of the American Society with the Institute, a program was developed which brought the state and national organizations so closely together that a sense of identity was created, and on a wholly voluntary basis they functioned as though they were parts of one organization.

These steps, taken over a period of years, were briefly as follows:

1. Presidents or other designated representatives of the state societies were made ex officio voting members of the Institute's Council, its governing body.

2. The Council was enlarged to give every state, no matter how small its population, at least one elected member of Council in addition to its state society representative. States with larger populations were entitled to additional Council members in proportion to the number of Institute members in those states.

3. The spring Council meetings were extended to four days, and were usually held at resort hotels away from large cities. Wives were encouraged to attend. This brought together leaders of the profession from all parts of the country, in an environment conducive to friendly social interchange, with time enough for extensive reporting, discussion, and debate on professional problems.

4. A state society service department was created as an arm of the Institute's staff. The department's responsibilities were to keep state societies informed of what the Institute was doing, to encourage their co-operation in joint efforts, and to assist the state societies in every way possible—in dealing with legislative problems, in arranging programs, in providing speakers, in suggesting committee activities, and so on.

5. The employment of full-time state society executives was encouraged; without such executives the constant turnover of state society officers hampered communication and continuous co-operation between the Institute and the societies. In addition, the Institute's experience suggested that the state societies could accomplish more if they, too, had full-time staff help.

Largely as a result of the Institute's encouragement, all the larger societies and many of the medium-sized ones developed full-time staffs, some of them of substantial size. Many of the smaller societies also acquired part-time or full-time staff assistants.

6. The Institute arranged annual meetings of state society executives, which resulted in close personal rapport between them and the Institute's staff. Meetings of state society presidents were also held separately from the meetings of the Council. These meetings later developed into an annual leadership conference, at which both presidents and principal staff of the

state societies were joined by an Institute committee on state society relations, its officers, and a number of its principal staff members.

7. A regular program of field trips by Institute officers and staff was established, through which most states were visited by an Institute representative at least once every two years, and in many cases annually.

8. Minutes of Council and executive committee meetings were sent to state society executives, and a state society newsletter was published to keep them informed of matters of current interest.

9. The bylaws were amended to authorize the state societies to submit a list of candidates to the Institute's committee on nominations from which it could select nominees for election to Council by the membership.

10. Following World War II a program of regional conferences was undertaken. The Institute took the initiative in organizing groups of state societies in the several regions of the country, which sponsored biennial or annual meetings of members in all the constituent states. These regional meetings permitted Institute officers and committee chairmen to meet face-to-face with large numbers of CPAs in each region.

11. In later years, the Institute sponsored conferences on state legislation and professional ethics, and invited officers of state societies and members of their related committees. These conferences were so successful that similar meetings on other subjects were proposed.

12. The annual meetings of the Institute were held in cities in various parts of the country, rather than only in the large metropolitan centers where hotel and entertainment facilities might be more readily available. This enabled large numbers of members to attend an annual meeting conveniently when it happened to be within a reasonable distance of their own residences.

By all these means communications between the Institute and the state societies were vastly improved. As a consequence,

a united approach to achievement of the profession's goals was greatly facilitated.

From time to time individual state societies, sometimes supported by others, challenged Institute policies or actions. These challenges ultimately were resolved in the Institute's Council, where the state societies were well represented. Sometimes proposals supported by the Institute's executive committee have been defeated, and on other occasions they have survived the challenge. In either event, the experience has been a healthy one, the problems have been ventilated, misunderstandings have been cleared up, and decisions have been made.

All in all, the Institute and state societies worked together so well that both came to consider themselves as parts of one whole—the organized accounting profession.

Membership Relations

As an independent entity, however, the Institute had to attract and hold together its own membership by its own efforts. The rapidly increasing diversity of interests among CPAs made this task difficult.

The larger firms, for example, were vitally concerned with SEC requirements, and the development of generally accepted accounting principles and auditing standards. Yet these matters were not of such immediate interest to some smaller firms, which were more concerned with the need for local recognition, public relations, information and education, and assistance in the management of their own practices.

In addition, a growing proportion of the membership was not engaged in public accounting. Many CPAs who had become corporate executives, government officials, or teachers of accounting also desired identification with the Institute, and service from it.

A balance of membership services was obviously required to maintain a united profession.

By 1945 demand for more attention to the problems of the

local practitioner seemed to be mounting. In that year the secretary reported to the Council:

> At least half of the Institute's members, for example, are probably more interested in having their local bankers understand auditors' reports than they are in the current accounting rulings of the SEC. Many members are more interested in taxation than in presentation of corporate financial statements for stockholders. The Institute cannot afford to neglect any of these important matters. Year in, year out it should try to maintain a balanced program so that no member will have difficulty in discerning among the Institute's activities something of direct interest or value to himself.

Advisory Committee of Local Practitioners

To consider this problem, an advisory committee of individual practitioners was appointed some years later, with two basic objectives: first, to develop a program to meet the needs of individual practitioners; and second, to help publicize the services of the Institute available to local practitioners, and stimulate their interest in the Institute.

Robert E. Witschey became chairman in 1951. As noted earlier, he was head of his own firm in Charleston, West Virginia. He had demonstrated leadership capacity as a participant in the Middle Atlantic States Accounting Conference. Later, he accepted many responsible assignments in the Institute and became president in 1962.

At his initiative, the committee reviewed all the major programs of the Institute and agreed on recommendations for expansion or modification of some activities to enhance their value to local practitioners.

Public relations was emphasized. In its report to the Council the committee said, "The growing dispersion of certified public accountants into smaller communities where no CPA has prac-

ticed before has given added reason for public-relations activities designed to make the general public more aware of what the CPA is and what he does. We strongly recommend as much expansion of these public-relations efforts as the budget will permit."

The committee also strongly advocated preparation of a handbook on the management of an accounting practice. This project was already in the incubation stage under the supervision of a separate committee (see Chapter 11), and the Witschey committee's support undoubtedly helped to bring it to fruition.

The size of this committee was gradually enlarged until it included at least one member from every state. Its meetings were heavily attended. Its discussions developed many useful proposals and provided helpful insights into the attitudes and desires of the local practitioners.

Many of the committee's recommendations were adopted. Local practitioners were given heavier representation on Institute committees, which brought their point of view directly into the centers of policy formation. This, together with enlargement of the governing Council, led ultimately to the conclusion that local practitioners were well represented in every phase of the Institute's work and in all policy decisions. It appeared that the job of the advisory committee had been completed, and it was therefore discontinued.

These efforts enormously improved relations between the Institute's management and the local practitioners in the membership. That membership, however, increased dramatically. By 1956 it had grown from 10,000 to nearly 30,000 in a decade. Despite everything that had been done, communications with so large a group were increasingly difficult. The extension of large firms with offices throughout the country, the increasing number of mergers of local firms with larger ones, and the occasional loss of clients by local firms to larger firms caused unhappiness among some local practitioners, and some of their displeasure rubbed off on the Institute.

Large Firms Consulted

When Marquis G. Eaton became president of the Institute, he took it upon himself to call a meeting of the senior partners of the largest firms in the country for a frank discussion of the local firms' problems. The attitude of the national firm partners was wholly co-operative. After extensive discussion, and the development of all available information on the subject, there was general agreement that some branch-office partners and managers had not been skillful in their relations with local practitioners. It was agreed that national firms should communicate with local firms if approached by one of their clients. It was also agreed that local representatives of national and regional firms should participate actively in the work of state societies and their chapters. There was no dissent to the proposition that publications describing a firm's services should be distributed only to existing clients or others who specifically requested it—a limitation already observed by the firms represented at the meeting.

It was clear that nothing could be done about mergers, which occurred only when they were to the economic advantage of both the smaller and the larger firm.

It was suggested that a system of referral would enable larger firms to assist local firms which were not able to provide some specialized services. To protect the local firm against additional invasion of his practice by a larger firm which he might call in to render a specialized service, it was proposed that a rule of ethics be adopted. This resulted in amendment of the Code of Ethics to provide that a member who received an engagement by referral could not discuss or accept any extension of his services beyond the specific engagement without first consulting the referring member.

There were differences of opinion at the meeting about the propriety of pamphlets, films, and books issued by larger firms which might have the appearance of promotional materials. It was agreed that if these materials were useful from a technical point of view, and if their distribution was limited to

clients or others who specifically requested them—or, in the case of books, were distributed through commercial publishers—there could be no valid objection to them. (Later, however, Robert M. Trueblood, as president of the Institute, proposed that technical materials produced by firms be published through the Institute for the benefit of the whole profession, and in some instances this was done.)

At the meeting of large-firm partners with President Eaton, there was also lengthy discussion of recommendations by investment bankers that companies "going public" change from local to national firms as auditors. It was agreed that an effort should be made to educate bankers as to the undesirability of displacing existing auditors when their competence could not be challenged, and also to assist members in retaining clients under such circumstances.

As a result of this and subsequent meetings, the executive director was authorized to publish a column in *The CPA* stating the desire of the larger firms to co-operate with local firms and with the Institute and state societies. The column invited members to complain about any questionable action on the part of a large-firm representative: the executive director would then report the incident to the senior partner of the firm concerned, with assurance that the incident would be investigated.

In response, few complaints were received. Several of these had merit, and appropriate action was taken by the firms concerned. Other complaints were found after investigation to be the result of misinformation or misunderstanding.

The Bankers' Influence

The influence of bankers in switching clients from local firms to larger firms was the subject of consideration for several years thereafter. One cause of concern was a common provision

in bond indentures for audit of the financial statements of the issuing companies by "nationally recognized" firms of accountants. This phrase was interpreted by many bankers as meaning one of the so-called "national firms," with offices in all parts of the country.

The Institute's executive committee finally adopted a resolution to the effect that "nationally recognized," when applied to accounting firms, should signify those firms whose competence, responsibility, and ethical standards had been nationally recognized: therefore, that firms composed of members of the Institute should be regarded as having attained national recognition. This resolution was communicated to law firms handling a large volume of corporate business and to leading investment bankers.

In 1960, J. S. Seidman, senior partner of Seidman & Seidman, was president of the Institute. He published an article in *The CPA* advising local firms how to minimize displacements resulting from banker recommendations. His principal suggestions were to establish personal acquaintance with the investment banker; to secure the client's co-operation in insisting that his present auditors be retained; but, if the use of a national firm was inevitable, to arrange to retain one through the initiative of the local firm itself, with the understanding that the local firm would continue to serve the client after the issuance of securities was completed.

In 1962, John W. Queenan, senior partner of Haskins & Sells, was president of the Institute. He, too, published a column in *The CPA* advising local firms on how to avoid displacement under similar circumstances. He also stressed personal acquaintance of partners of local firms with officers of commercial and investment banking houses. He cited facts to demonstrate that many local firms had been successful in retaining clients whose securities had been publicly issued. His analysis of 708 prospectuses of commercial and industrial companies showed that 254 different accounting firms had audited one or more of these companies. Mr. Queenan's conclusion was that the reports of a local accounting firm would generally be acceptable

to underwriters if the firm became acquainted with them and demonstrated its capabilities.

A year later the Institute sent a printed circular letter to the 15,000 members of the American Bankers Association and to members of the Investment Bankers Association. Enclosed was a geographical list of all accounting firms represented in the Institute, and of individual practitioners who were members. The letter pointed out that each firm listed was subject to the Institute's Code of Ethics.

The Code was summarized in a supplement to the letter, stressing the rules on independence, technical standards, reporting standards, advertising and solicitation, and confidential relationship. The procedures for enforcement and the activities of the practice review committee were briefly described.

The supplement also described the standards of competence embodied in the requirements for the CPA certificate, and the nature of the Uniform CPA Examination.

The competence of local firms was stressed: "It should not be assumed, simply because a firm name may not be known to you, that the quality of its work is in any way inferior to that of others." The disadvantages of displacement of local firms without good reason were cited.

The Institute offered to respond to inquiries from bankers to the best of its ability.

In later years officers of the Institute communicated directly with bankers who were said to have recommended that national firms replace local firms in specific situations. In every case the principal executive officer of the bank concerned stated that any such action was contrary to the bank's policy and would not be repeated. Individual members were also advised by correspondence on how to minimize displacements in circumstances such as those indicated. In a number of these cases, the local firm was successful in retaining its client.

A professional development course on SEC filings, sponsored by the Institute, supplemented these efforts. Many representatives of local firms attended sessions of this course, which was given in various parts of the country.

Future of the Local Practitioner

The future of the local practitioner was discussed by Marvin L. Stone, president of the Institute from 1967 to 1968, in a *CPA* column for July-August 1968.

Mr. Stone, head of the local firm of Stone, Gray and Company in Denver, noted that during the 20 years from 1946 to 1966 the number of CPAs associated with the ten largest firms had jumped from 2,950 to 11,850—a 401 per cent increase. However, the total number of CPAs had jumped from 20,778 to 94,284 during the same period—a 453 per cent increase. He said that while mergers of local firms with larger ones made news, the constant formation of new local firms did not attract so much attention.

Mr. Stone also pointed out that while big business was getting bigger, reputable economists offered statistics to show that small business was maintaining its relative position in the economy—and in fact had probably improved it. He cited a Brookings Institution study which said, "The growth of big business appears to have been matched . . . by growth of the economy as a whole, with no material alteration of its place in the whole content over the past quarter century."

Mr. Stone did express the opinion that the average local accounting firm would tend to grow larger as the demand for a wider range of services increased, and that many sole practitioners and small firms would band together either in partnerships or informal groups.

Other studies supported this prediction. Mergers among local firms were at least as numerous as mergers of local firms with national firms. Meanwhile, new national firms emerged as a result of acquisition of local firms or mergers of regional or semi-national firms.

In short, while recognizing a trend toward practice units of larger size, neither Mr. Stone nor other students of the subject found any basis for predicting the demise of local accounting firms as a class. These conclusions assumed that such firms would maintain acceptable competence.

Membership Services

From 1936 onward the Institute recognized that preservation of a united profession required attraction and retention of a substantial proportion of the certified public accountants of the nation in both the national and state professional societies.

In the original societies of Scotland and England, and in the British Commonwealth countries which had patterned their structures after the originals, membership acquisition and retention were no problem. The societies were accrediting agencies. They conferred the title Chartered Accountant on those who met their requirements and became members. Those who ceased to be members no longer had the right to use the title.

But in the United States the CPA designation was conferred by state boards of accountancy under state law. No CPA was required to be a member of any professional society. Membership was voluntary, and resignation or dismissal had no effect on the right to practice as a CPA.

Even after the merger of the two national organizations in 1936 the Institute had only about 5,000 members. There were about 16,600 CPAs in the country at that time. A national organization which included only less than one-third of the qualified members of the profession could hardly claim to represent the profession as a whole.

Up to 1936 many local practitioners found membership in their state societies sufficient for their needs and saw no reason to pay dues to the Institute. It was remote; it was thought to be mainly concerned with problems of the big firms; it arranged no local meetings; its publications could be purchased for less money than the annual dues. Why join?

A conscious effort to answer that question was made by expanding the scope of membership services. The objective was to convince the individual members of a rapidly growing and heterogeneous profession that the national organization offered each of its members some service that would make it worthwhile to pay his dues.

Library and Information Service

The Institute's library rendered invaluable service to the members, to students, to accountants in other countries, to the Institute's staff, to business corporations, and to educational institutions. It housed a complete collection of published works on accounting and related subjects. Countless researchers spent hours, days, weeks, and months within its walls. Books and magazines were loaned to thousands of members. Inquiries answered by the library mounted to astonishing numbers.

The following numbers indicate the growth of the total service:

	Total Collection of Books Magazines, etc.	Total Number of Publications Loaned to Members	Total Number of Inquiries Answered
1937	14,780	2,309	9,901
1967	52,396	15,888	37,239

The *Accountants' Index* and supplements, prepared and published by the librarians, were a source of reference for many thousands of accountants, students, and accounting teachers.

In 1952, a technical information service was inaugurated. This service, maintained by a full-time staff assistant trained in accounting, provided answers to technical questions which the librarians were unable to answer by reference to published sources. For obvious reasons it was impossible to answer tax questions. The service proved of great value, particularly to members in smaller accounting firms whose research facilities were limited.

Selected questions and responses appeared from time to time in a section of *The Journal of Accountancy,* and later were published in book form, the most recent edition of which appeared in 1966 as a three-volume work entitled *Practical Accounting and Auditing Problems,* prepared by Edmund F. Ingalls, then manager of the technical information service.

Publications

Following the merger in 1936, the circulation of *The Journal of Accountancy* began to climb. In 1936 it was 8,325; a year later it was 11,014. Following World War II, under four successive editors—William Papworth, John Lawler, Charles Noyes, and William Doherty—the circulation mounted steadily from about 25,000 to a high of about 125,000 in 1969.

As resources permitted, editorial content was improved by the addition of regular departments on taxes, education, accounting and auditing questions, management services, and practice management; by expansion of news coverage; and by the active solicitation of articles on topics of current interest.

Changes were made in the format of the magazine from time to time to enhance its readability and to keep up with current styles in magazine publishing. One of these involved a change in size, from the traditional 6″ × 9″ page to an 8¼″ × 11¼″ page which would more readily accommodate typical advertising layouts. Some readers complained about this break from tradition. One of them wrote, angrily, that he could no longer put the magazine in his bookcase. "What," he asked, "am I to do with it?" To this the editor responded, "Why don't you try reading it?"

More than 50 per cent of *The Journal* subscriptions came from non-members of the Institute: corporate officials, bankers, lawyers, government officials, teachers, and students. Thus *The Journal* ceased to be a "house organ," and became both an educational and a public-relations medium for the accounting profession, whose messages reached a large audience outside of its own membership.

The monthly membership bulletin, later named *The CPA,* informed the members of what the Institute was doing, and included comment from officers and members. It provided direct communication between the rapidly growing membership and the "headquarters" organization. It also relieved *The Journal of Accountancy* of the necessity of publishing

material that would not have been of interest to non-member readers.

In 1964 the Institute added to its list of periodical publications a new magazine entitled *Management Services,* edited by Robert M. Smith. This specialized publication was directed toward accountants in public practice and in industry who were concerned with the more advanced techniques in the evolving fields of electronic data-processing, information systems, operations research, and related subjects. As expected, the circulation proved to be limited, reaching a level of about 20,000. However, the magazine attracted the support of some of the leaders in the field of management sciences, and it identified the accounting profession as one of the groups actively interested in this area.

As noted in Chapter 15, publication of a new periodical, *The Tax Adviser,* was begun in 1970.

The publication of books was also an important part of the Institute's program. It was the general policy not to publish books that would compete with those of commercial publishers, but to produce only works that evolved naturally from the activities of the Institute itself or were of such limited interest that commercial publishers would be unlikely to undertake their production. Prominent among these books is the annual *Accounting Trends and Techniques,* first published in 1948, which analyzes the financial statements of some 600 prominent corporations selected from among basic industry groups. Through this annual publication, trends in financial-reporting practices were highlighted, and it became possible to measure improvement over the years.

Among the other publications of the Institute were the technical pronouncements on accounting and auditing (the former embodied in a loose-leaf service in 1968), manuals on the management of an accounting practice and management services, and books on professional ethics and educational policies.

By 1969 the list of books and pamphlets then available had increased to nearly 60 items.

Continuing Education

Inauguration of the professional development program (described in Chapter 11) was an enormous encouragement to membership growth and retention. This program brought together thousands of members under the Institute's banner. Since most of the courses were jointly sponsored by the state societies, the program also provided vivid evidence of the co-operative relationship existing between the state and national organizations. The value of the courses to participants has been freely and widely acknowledged.

One local practitioner in Tennesssee remarked that despite complaints of some of his colleagues about what the Institute was doing or failing to do, so long as the professional development courses and the technical information service were available to them they could not afford to dispense with their membership.

Insurance Plans

Of direct financial benefit to members were the group life-insurance plan and the retirement plan developed by the Institute.

The group life plan was created in the mid-1940's, when a change in the New York insurance law—reportedly motivated by labor unions—made it possible for membership associations to provide insurance at group rates to members and their employees.

In 1948, the first full year of operation, 793 firms participated, insuring 5,587 lives. The total insurance in force was $26,800,000. By 1958, 3,516 firms were participating, insuring 21,832 lives, and the total coverage amounted to $333,800,000.

The plan was supplemented in 1958 by provisions whereby individual CPAs could obtain coverage. By 1968 nearly 22,000

individuals were covered in an aggregate amount of $491,500,-000, which when added to the coverage purchased by firms, brought the total to more than $825,000,000. The monthly net cost for a thousand dollars of life insurance in the group insurance plan for 1969 was 44 cents, and the total amount of insurance in force was approaching a billion dollars.

A retirement plan for members and their employees was also developed by the Institute and launched in 1964. Five years later, participations were approaching 3,000.

These plans had a strong influence in holding the membership together.

Action in Washington

The so-called Keogh Bill, which made it possible for self-employed individuals to deduct from taxable income limited amounts set aside for their own retirement, encouraged participation in the Institute's retirement plan described above.

Together with the American Medical Association and the American Bar Association, the Institute was a major force in achieving enactment of the Keogh legislation. In the effort to persuade Congress to pass this law, in the face of stiff opposition, the Institute contributed a total of more than $50,000 and incalculable amounts of the time of its staff and members. State society officers and members also gave indispensable aid. The results were appreciated by nearly all members.

In other federal legislation also, direct benefits to the membership were achieved—notably in the defense of the CPA's tax practice.

The establishment of the Institute's Washington office greatly increased the flow of information from the nation's capital to Institute members, and accordingly brought to light many opportunities for useful service by CPAs which might not have been discovered before.

Practice Management

The economics of accounting practice—how to make a practice yield a sufficient income to maintain a CPA in dignity and permit him to develop his professional talents to the full extent—was a major concern of Marquis G. Eaton, when he attained the presidency of the Institute. He created a committee on the economics of accounting practice, which, with the help of Roderic Parnell, of the Institute's staff, produced bulletins designed to assist local practitioners on such subjects as fees and income, staff recruiting and retention, controls for the effective use of time, client relations, billing and collection procedures, and similar subjects.

Since the Institute's budget was inadequate to support this additional activity, it was necessary to offer the bulletins for sale. Seventy-eight thousand copies were sold, and the response from the membership was warm.

In 1960 the name of the committee was changed to committee on management of an accounting practice. It continued the publication of a series of bulletins on similar subjects, producing 17, with a total distribution of about 125,000 copies.

In 1962 materials in these two series of bulletins, plus other material published in the *Journal's* "Practitioners Forum" and elsewhere, were edited and reproduced in the *Accounting Practice Management Handbook,* a publication of 952 pages, covering all phases of the management of a practice.

Management Services

The initial objective of the first committee on management services was to encourage local accounting firms to extend their practices into areas already explored by the larger firms. The committee's first bulletins contained a classification of management services performed by CPAs, and a discussion of the

general nature of such services, emphasizing the normal extension of accounting and auditing service into areas of management concern. The first technical bulletin in this series was on budgeting.

As the level of sophistication of the profession rose, the committee undertook a series of more advanced technical studies. Subjects covered included cost analysis for product-line decisions and for pricing and distribution policies; analysis for purchasing and financing productive equipment; and inventory controls and forecasting techniques. A booklet entitled "Guidelines for Administration of a Management Advisory Service Practice" was also produced in 1968. Bulletins on the nature of management services and competence in this field appeared in 1969.

The Computer Program

In the early 1960's, it became evident that the rapid advances in computer capabilities would have a tremendous impact on the practice of accounting in many ways. Through speeches and articles, the members were urged to familiarize themselves with this new facility, but the Institute provided no means of acquiring such familiarity. No one on the permanent staff was a computer expert, and the amount of time that committee members could devote to educational activity was limited. Accordingly, in 1965 a contract was signed with the Systems Development Corporation to act as a consultant in a research and educational program.

The first step was a questionnaire sent to firms represented in the Institute, to determine the extent to which electronic data-processing equipment or stored-memory computers were being utilized either through lease or purchase, or through service bureaus. The result indicated an alarming lack of infor-

mation, and in some cases even of interest in the subject, on the part of local firms.

It was decided to publish a series of bulletins on the basic aspects of computers as they might affect accounting practice. The first bulletin summarized the survey results; the second listed basic sources of information on the subject; the third dealt with accounting applications of computers; the fourth dealt with the relationship of banks and CPAs in computer accounting; the fifth discussed software trends, and the sixth concerned an approach to the uses of EDP in a small accounting practice.

More than 193,000 copies of these bulletins were distributed to the membership free of charge, and nearly 17,000 copies were sold. The impact was noticeable. Members' interest in acquiring knowledge about computers was visibly heightened.

Professor Gordon Davis, a CPA and head of the computer center at the University of Minnesota, was retained on a year's leave of absence to pursue the program.

His major contribution, accomplished with the aid of a team of experts assembled from the membership, was the production of the most authoritative manual on auditing computerized records developed up to that time, entitled *Auditing and EDP*. Professor Davis also assisted in the preparation of professional development courses on computers, which attracted wide participation.

The growing interest in the use of computers by local accounting firms led to the formation of a so-called "users group" within the Institute which, with the assistance of a full-time staff assistant drawn from industry, arranged a series of conferences on computer technology, and developed plans for the exchange of information among members who utilized the equipment.

Professor Davis also arranged with the Auerbach Corporation to publish a special edition of its *Computer Notebook* for members who were interested in keeping up with trends. More than 2,000 public accounting firms represented in the membership subscribed to this additional service.

Evaluation of Audit Capacity

Persistent reports of instances where bankers had encouraged clients of local firms to change to larger and better-known firms continued to cause concern. Protests and propaganda described earlier in this chapter had not solved the problem. "What to do about it" was put high on the agenda of the newly formed planning committee, whose activities are described in general terms in Chapter 18.

It was recognized that bankers were acting only in accordance with the dictates of human nature when they recommended firms with whose work they were familiar, and whose competence could be assumed. It was also recognized that while many local accounting firms were fully as competent to conduct opinion audits as the larger firms, there were also many local firms whose practices consisted largely of tax, general accounting, and advisory services. There was evidence that some of these latter firms did not keep up to date with evolving auditing standards and procedures.

The planning committee concluded that the audit of enterprises of any size and complexity had become a team job, rather than the exercise of personal professional skills of an individual. In other words, it was the competence of a firm or practice unit that banks would question, not the competence of an individual CPA who might be a partner or the sole proprietor of the practice unit. It was suggested that if there were some means of evaluating the competence of a firm as a whole to conduct independent audits, then those local firms which demonstrated competence might effectively resist displacement as a result of bankers' pressure.

A plan was developed under which the Institute might evaluate the audit capacity of accounting firms in accordance with a set of standards roughly similar in nature to those used in accreditation of medical schools, hospitals, and law schools. For example, it was proposed that the competence of staff be evaluated according to education, experience, training, and supervision; that the familiarity of partners and staff with

auditing standards and procedures be appraised; that working-paper techniques and internal quality controls be examined; that library facilities be checked; and that the attitude of the partners with regard to ethics and independence be tested. Firms which measured up to the standards might be given a symbol of accreditation which would be reassuring to the bankers, and firms which did not measure up would be given an opportunity to do so at another time. Firms or individual practitioners who saw no need for the accreditation would not be required to participate in the program. The objective was a voluntary effort to distinguish firms, as contrasted with individuals, as practice units which could be relied upon to perform independent audits at an acceptable level.

Recognizing that the idea was novel and radical, the proposal was explained in a column written by the executive director in *The CPA* of June 1967, with an invitation to members to express their views.

The result was an outburst of objection. Highly emotional and critical letters were received, some of which accused the Institute of attempting to downgrade the status of the CPA certificate, to discredit the local practitioner, and to divide if not destroy the accounting profession.

The negative opinion was overwhelming and the plan was dropped.

However, in spite of this discouragement, after further study the planning committee developed a variant of the idea. It suggested that the Institute provide facilities for a confidential review of the auditing capacity of any firm which desired it and was willing to pay the cost. A number of local firms had already expressed an interest in having such a review, simply as reassurance to themselves that their standards were satisfactory, or as a means of discovering weak spots which they could remedy. Under the revised plan no accreditation would be given, and there would be no publicity as to the success or failure of any firm to measure up to any preconceived standard. The firm which paid for such a review would receive a confidential report, and that was all.

This idea for "voluntary quality control in auditing" was exposed to the Council in 1968, and later approved by the executive committee. Implementation, however, required a good deal of planning and organization, and at the time of this writing the plan had not yet become operative.

The Attitude of Large Firms

It should be noted at this point that the larger firms consistently supported all the Institute's efforts to assist local practitioners. The library and the original bureau of information were financed by large firms in 1917, not because they needed these facilities, but for the benefit of the membership throughout the country.

Larger firms made their own staff-training materials available to the Institute's professional development division, which adapted them for the use of local firms.

The larger firms contributed $80,000 to launch the personnel testing program (see Chapter 11).

They contributed hundreds of thousands of dollars to support the accounting research program and the work of the Accounting Principles Board.

They furnished manpower for committee work and consultation in all technical and professional areas, which at regular rates would have represented a cost of millions of dollars.

In these and many other contributions, the partners of the larger firms were motivated by a sense of responsibility to the profession of which they were a part.

In addition, the senior partners of large firms recognized the desirability of a united profession. It would not be in their own interests to have the CPAs of the country divided into two competing groups, as they had been in the period from 1921 to 1936. It was greatly to the advantage of the larger firms, as well as the smaller ones, to have the profession speak with one voice in Washington. An organization of nearly 70,000

members obviously could be more influential than a smaller one—or than two smaller ones whose attitudes on some questions might be in opposition.

Furthermore, the larger firms had vital interests which required an organization through which they could co-operate with medium-sized and smaller firms in the solution of problems which no one firm, no matter how powerful, could solve alone.

For example, the time had long since passed when each firm could decide for itself what were acceptable accounting principles. It had also long since become apparent that if the profession as a whole did not issue authoritative pronouncements on auditing standards and procedures, the ultimate decisions would be made in the courts in cases in which accounting firms were sued for negligence. The support of a united profession had proved useful in cases in which an accountant's legal liability threatened to be extended beyond tolerable bounds. The development of professional policies relating to scope and standards in the relatively new field of management services was also of immediate concern to the larger firms who pioneered in this area.

To some extent, of course, the larger firms also benefited from many of the Institute's services which have already been mentioned.

In addition, another opportunity for Institute activity, particularly useful to large firms, emerged from the widening practice by American accounting firms in the international arena.

International Affairs

World War II left the United States as the principal source of capital in the world. Americans invested in foreign enterprises. American corporations established plants, divisions, and subsidiary corporations in South America, Europe, Africa, and Asia, and the multi-national corporation emerged.

American accounting firms serving the larger corporations found it necessary to establish offices, or to develop correspondent relations with foreign firms, in all parts of the world in order to serve the expanding needs of their giant clients.

However, efforts to establish new offices or, in many cases, even to maintain offices established many years before, were impeded by the nationalistic attitude of governments or the organized accounting profession, or both, in the countries concerned. The alternative, to establish correspondent relations with foreign firms, required assurance that the accounting and auditing standards of such firms were equivalent to those established in the United States. This was essential both for purposes of registration of issues with the Securities and Exchange Commission and for protection of the reputations of American accounting firms whose opinions appeared on financial statements audited in part by foreign correspondents.

Through a reactivated Institute committee on international relations, a vigorous program was undertaken to encourage international co-operation among professional accountants, to improve exchange of information, and eventually to agree on common standards.

American accountants attended in large numbers and took an active part in the International Congresses of Accountants held in London in 1952, Amsterdam in 1957, New York in 1962, and Paris in 1967.

At the New York and Paris conferences, spokesmen from other countries proposed more frequent international meetings of smaller groups; better exchange of information on accounting and auditing standards; establishment of an international secretariat; and closer co-operation among bodies in various countries.

At Paris, an international committee was appointed to explore these possibilities. The United States was represented on the committee by Clifford V. Heimbucher, past president of the Institute and an active participant in the Paris congress. At the time of this writing the conclusions of this committee had

not yet been reached, but it seemed possible that they would in time lead to some significant developments.

In the meantime, the firms represented on the Institute's committee on international relations produced a pioneer work, *Professional Accounting in 25 Countries,* which was published by the Institute in 1965. This book, based on extensive research, compared the qualifications for admission to the profession and the prevalent accounting and auditing standards in 25 highly industrialized countries.

Perhaps partly stimulated by the appearance of this work, the president of the Institute of Chartered Accountants in England and Wales proposed, at meetings of the Canadian Institute of Chartered Accountants and of the American Institute of Certified Public Accountants in 1966, that representatives of the three countries undertake joint studies comparing current accounting and auditing practices in Canada, the United Kingdom, and the United States. These studies were intended to provide a basis for comparison and discussion. The first study, "Accounting and Auditing Approaches to Inventories," was published in 1968. Two more, "The Independent Auditor's Reporting Standards in Three Nations," and "Reliance on Other Auditors," were published in 1969.

In January 1966, the Institute's committee on international relations, under the chairmanship of James J. Mahon, partner of Lybrand, Ross Bros. & Montgomery, prepared a statement on accounting aid to developing countries, suggesting a program to improve accounting in nations where an industrial economy was emerging. This policy statement was submitted to international finance and lending institutions, with a request that they appoint representatives to serve on a committee to formulate and carry out such a program.

In April 1966, as a result, the International Committee for Accounting Co-operation (ICAC) was established. In addition to representatives from the Agency for International Development, the Inter-American Development Bank, the International Finance Corporation, the International Monetary Fund, and the

Pan American Union, the committee was composed of representatives from the national professional societies of public accountants in Canada, Mexico, and the United States. Theodore L. Wilkinson, partner of Price Waterhouse & Co., who succeeded Mr. Mahon as chairman of the Institute's committee on international relations, became the ICAC's first president.

In the first phase of its program, the ICAC, with financial support from organizations represented on the committee and several accounting firms, undertook a pilot project aimed at improving accounting education and upgrading professional standards in a developing country. A preliminary survey was conducted in the country selected as the site for the project. The results of the survey indicated that an investment of over a million dollars would be required to accomplish the desired results.

In the absence of foundation support for such a massive program, the ICAC focused its efforts on seeking scholarship aid for training accounting professors from other countries in the United States, translating and publishing accounting literature in Spanish, and preparing continuing-education courses. It was hoped that these steps would accelerate accounting development throughout Latin America.

On another front, the Institute committee produced pamphlets designed to elicit the support of bankers and investors in the United States, as well as foreign governments and accounting organizations, for the efforts of American accounting firms to maintain offices in foreign countries where American capital had been invested. The argument was basically simple: if American capital was to be invested abroad, American investors required reliable reports of the progress of the enterprises.

To sum up, the Institute attempted to make itself a vehicle through which its members, in firms of all sizes, could accomplish on a co-operative basis what could not be accomplished by individuals or firms acting alone, and to render a variety of

services among which each member could find something of value to him.

Evidence that some success attended these efforts appears in these statistics: (1) the membership increased from 4,890 in 1937 to more than 70,000 in 1970; (2) while only 30 per cent of all CPAs were Institute members in 1937, more than 60 per cent of the much larger CPA population were members in 1970; and (3) losses of members through resignation and non-payment of dues were averaging less than 2 per cent a year.

A secretary of the Institute of Chartered Accountants in England and Wales once remarked that the American Institute's growth was remarkable in view of the fact that membership was wholly voluntary.

Nevertheless, tension between small firms and large firms continued to exist. As late as 1968 a speaker at the Institute's annual meeting sharply criticized larger firms on several counts—and was applauded. Human nature being what it is, this tension will probably never be fully eradicated. But it can be prevented from erupting in a manner which would damage the profession as a whole—both small firms and large.

As the numbers of members in both the Institute and the state societies continued to increase at a rate which suggested that they would soon pass 100,000, efforts were intensified to maintain effective communications, to expose policy proposals before they were adopted, to encourage membership reactions, and to audit the performance of the professional organizations, both their committees and their staffs.

The history of the profession, and the attacks on many of society's institutions in a rapidly changing environment, suggested that underlying tensions could be ignored only at the risk of dividing a united profession.

CHAPTER 14

Public Service and Public Relations

As THE organized profession entered the period of its explosive growth, the subject of public relations became of even greater concern than formerly. Some of the earlier efforts to achieve greater visibility have been described in Volume I of this work. But frustration at the lack of adequate recognition became more intense as the CPAs became more numerous and the scope and significance of their services increased. They knew that they were not receiving half the credit they deserved for the contribution they were making in the areas of financial reporting, taxation, and special services to management. Their opportunities for public service were limited because so few people, relatively, knew what CPAs could do.

Among local firms there were frequent complaints that the public generally did not distinguish certified public accountants from non-certified accountants. Recruiting efforts were handicapped by the failure of many students and their parents to distinguish accounting from bookkeeping. Few business men seemed to be aware of the constructive services to management

which CPAs could provide, and often turned to management consultants for assistance which their accounting firms were equipped to render. The press appeared indifferent to the activities of the organized professional accounting societies, which were frequently disappointed at the failure of newspapers to report their meetings and other activities.

More important, in view of the powers vested in the SEC, was the need for public understanding and support of the profession's efforts to set its own standards in the areas of financial reporting and auditing.

What was happening, of course, was that the rapid growth of the profession was out-pacing public awareness. There is always a time lag in public comprehension of rapid change. Furthermore, the profession had not yet developed adequate means of communication to bring public opinion up to date. Even when the Institute's membership passed the 10,000 mark in 1946, its resources were limited. Neither the state societies nor the Institute had the money to embark on any large-scale program of public information.

Another handicap was the fact that neither the professional societies nor the individual members, with a relatively few but notable exceptions, were prominently involved in activities of interest to the general public which could be considered "news."

Nevertheless, the need for better public relations could not be ignored, and as the membership and revenues increased more money was invested to this end.

Early Public-Relations Efforts

Ever since the 1920's the Institute's staff had included at least one man with a journalistic background, who was responsible for issuing press releases on activities which it was hoped had some news value. After World War II the public-relations staff was augmented, and outside public-relations con-

sultants were engaged to assist in the development of a broader program.

The problem was complicated, however, by differences of opinion about the goals. Some members simply desired to get the profession's name in the paper for personal satisfaction and possible enhancement of status. Others assumed that public-relations efforts should be designed to expand the economic opportunities of CPAs. Still others were most interested in developing a favorable climate of public opinion to gain support for the profession's long-range objectives: the best example of the need for such support was the controversy over tax practice described in Chapter 9.

To the best of its ability, the Institute tried to satisfy all these desires.

Analysis by the public-relations consultants disclosed that the relatively meager reports of the profession's activities in the newspapers were largely due to the profession's inexpertness in dealing with the press. For example, the day had passed when newspapers would send a reporter to attend a meeting and write his own story of the proceedings—unless a speaker of prominence was to be heard or a question of general interest to the community was to be discussed, and sometimes not even then. It was necessary for the organization conducting the meeting to prepare a press release describing what transpired at the meeting, and to get the release in the hands of the editor in time to meet his deadlines. It was also desirable to become personally acquainted with editors and reporters—to provide them with sufficient background to understand the significance of accounting developments to the general public.

The Institute prepared a manual for the information of state societies, as well as its own staff, covering the how-to-do-it of press relations. This manual has been revised from time to time, under titles such as "Press Publicity and How To Get it." Many of the state societies employed public-relations assistants on a part-time basis to aid in their press relations, and the results showed noticeable improvement.

The Institute, too, expanded its efforts. Annual meeting

programs were tailored in part to attract favorable press attention. "Home-town releases" were sent to local newspapers in cities in which members elected to the Council or appointed to Institute committees resided. This effort was based on the assumption that "little drops of water" would have a cumulative impact on public consciousness—that people would gradually become aware at least of the existence of an organized profession of CPAs.

New pamphlets were prepared on accounting as a career. While designed primarily for students, it was hoped that these materials might also be read by teachers and parents. As noted earlier, several films on accounting as a career were also released.

In the forties and fifties the Institute's staff produced a series of "hard sell" pamphlets, and articles for trade and business publications, frankly designed to encourage readers to use the services of CPAs.

In 1947 there was even a brief experiment with paid advertising—over the objections of a minority. An advertising agency was retained which, with the help of the Institute staff, developed a series of brief messages about the profession. The titles included "Good Business Calls for Good Accounting," "How Good Is an Opinion?" "How Much Did You Make Last Year?" and "Taxes and Accounting Problems." The advertisements were offered to state societies for use in local publications, with the understanding that the societies would pay for the advertising space. At first the program was received with some enthusiasm, and some of the messages were published in several states.

The Texas Society of Certified Public Accountants, however, having expended some $12,000 on the program, wisely decided to check up on the results. A readership survey of business and professional people was conducted in one of the cities in which the ads appeared. The disappointing finding was that only about 4 per cent of those queried had read the messages, and 82 per cent were not even conscious of the fact that they had appeared. This was persuasive evidence that the

cost of paid advertising was greater than the results were likely to justify. The advertising program was abandoned.

Beginning in 1949, the Institute provided state societies with short recorded messages on income taxes, to be used by local radio stations as a public service, with the societies named as sponsors.

For several years the Internal Revenue Service co-operated with the Institute in these radio programs, and on occasion the Commissioner participated in the recorded dialogue. Later, video-taped television shorts of a similar nature were provided. These messages were widely used and undoubtedly reminded millions of listeners and viewers that certified public accountants were adept in taxes. However, in order to achieve wide exposure the messages themselves had to deal with the simple tax problems of ordinary citizens. This evoked objections within the profession to the implication that CPAs were mainly concerned with individual, rather than business, taxes.

A number of the state societies and the Internal Revenue Service were developing their own televised tax programs. Tax messages were also prepared, both by the Institute and some state societies, for publication in the local press, and these were well received. The utility of the Institute's radio and TV shorts, in the light of the substantial investment required to produce them, came into question and the program was ultimately discontinued.

All these public-relations efforts were undoubtedly helpful. It is reasonable to assume that people knew more about certified public accountants than they would have if these efforts had not been made. On the other hand, the total impact on opinion of the American public as a whole is questionable. The measurement of results of public-relations activities is difficult and expensive. It requires surveys which may cost more than the original efforts. The questions of who reads or who listens, who understands what he reads or hears, and who remembers it or acts upon it are almost impossible to answer definitely.

These difficulties are compounded when the public-relations

objectives are not clear, and when there is no sustained, co-ordinated program designed to accomplish specific purposes. Resources may be dissipated without demonstrable results.

A New Look

As noted in Chapter 9, the Institute engaged Earl Newsom & Company in 1954 to advise and assist it in responding to the challenge to the accountant's tax practice. Earl Newsom, an acknowledged leader in the public-relations field, was an intensive student of public opinion and had been eminently successful as an advisor to some of the largest corporations in the country. It had been demonstrated to his satisfaction that it was impossible to "educate the public" as a whole on any subject. Most people, he said, would not receive information on subjects unrelated to their own immediate interests, and efforts to convey information, therefore, should be focused on the specific audiences whose interests were involved.

Furthermore, Newsom pointed out, communication of information is only one phase of the development of good public relations: the first essential is to *deserve* favorable public opinion and support, and this depends on the attitudes and actions of the organization itself. Policies and activities clearly in the public interest will attract favorable attention. Attitudes and actions which appear to be selfishly motivated, or contrary to the public interest, will attract unfavorable attention. An organization will be judged more by what it does than by what it says about itself.

The soundness of this reasoning was demonstrated, for example, by the extremely favorable reaction of the banking community to the Institute's issuance of Statement on Auditing Procedure No. 23, as described in Chapter 7. The profession had voluntarily imposed on itself more rigid reporting requirements, which were helpful to credit-grantors.

Earl Newsom also pointed out that very few organizations—the White House might be an exception—could expect to hold

the attention of the public, or very many segments of it, for long periods. But occasions arise when the spotlight of public attention falls on almost every important group for one reason or another. When the spotlight falls, what will the public see? Will it like what it sees? The implication of these questions is that self-examination is essential to maintenance of good public relations. Is the organization's house in order when visitors arrive? Will outsiders feel that the organization merits support?

In 1955 the Institute's executive committee asked Earl Newsom & Company to review the public relations of the accounting profession and of the Institute; to identify the points at which the problems of the profession should be attacked; and to recommend a general course which the Institute might follow to earn greater public understanding of the profession. The result was a memorandum entitled the "General Recognition of Accountancy as a Profession" by Arthur B. Tourtellot, then a partner of Earl Newsom & Company. This was a thoughtful, philosophical analysis, providing a basis for a broadened approach to public relations at a more sophisticated level. The memorandum was printed and distributed to the Institute's membership.

Later Public-Relations Efforts

The Institute's public-relations activities became more effective as its resources permitted retention of professional consultants and employment of experts in public opinion on its full-time staff.

In 1956, as an experiment, an annual report was issued, dealing with broad problems of interest to the outside world as well as to the membership itself—after the manner of foundations, university presidents, and other non-profit institutions. The first report of this kind was entitled "The Expanding World of Accounting." It attempted to relate the work of the profes-

sion to public needs. Copies were distributed to large numbers of "thought-leaders" outside the profession, in the hope that they would, so to speak, read over the members' shoulders.

For several years the annual reports were prepared along similar lines, the most ambitious of which appeared in 1959 entitled "The Financial Health of Small Business."

Thereafter, it was decided, however, that too much effort and expense in terms of staff time were involved in preparing annual reports of high quality, and that other needs had become more pressing. This series was terminated. Some ten years later, however, it was proposed that a new series of annual reports be undertaken, containing substantive material of interest to the public. At the time of this writing, the proposal was under study.

In 1963 the Institute produced a booklet on "Public School Costs," subtitled "An Accounting Primer for School Board Members and Taxpayers." This proved immensely popular. There was an initial free distribution to 14,000 school superintendents, and an additional 50,000 copies were sold. In 1965 a guide was prepared for state societies to use in conjunction with the booklet, particularly at meetings on school budgets, entitled "Telling the School Costs Story." State societies and their chapters made use of this material in many instances.

Encouraged by these successes, in 1967 the Institute distributed another pamphlet entitled "The Layman's Guide to Preparing Financial Statements for Churches," of which 90,000 copies were distributed; and in 1968 a pamphlet on "New Approaches in Public Education" was prepared for the guidance of school administrators, of which 10,000 copies were distributed. This dealt with budgeting, performance measurement, and management in public schools.

In addition to special activities of this type, the staff regularly released news items on Institute activities and assisted in arranging speeches by CPAs before business and professional groups—including such prestigious organizations as the Detroit Economic Club, the Credit Policy Committee of the American Bankers Association, the Institute of Chartered Financial Ana-

lysts, the National Industrial Conference Board, the Hayden-Stone Accounting Forum, and many others. Special articles were also prepared by the staff for publication in financial magazines, and assistance was provided to professional writers of articles about accounting.

Public Service

Among other things, the new approach emphasized public service, both by the professional organizations and by their individual members.

There were two fields of public service which the Institute had already exploited to some extent—tax legislation and administration, and federal government accounting. Its contributions in these fields will be summarized in the next two chapters.

But while the Institute was increasing the visibility of the accounting profession as a whole through its activities in the tax and governmental accounting areas, many individual members of the profession were enhancing its prestige by personal public service both at the local and national levels.

For decades the Institute had encouraged its members to take part in community affairs. In recognition of such service, brief descriptive items were published in the monthly *CPA*. Eventually, however, the volume of reports of public service by members became so great that space limitations prevented continuation of such notices. Members of the Institute by the thousands were serving as officers or directors of civic groups, service clubs, charitable organizations and hospitals, and in responsible positions on school boards, in churches, university alumni groups, advisory councils to business schools, and so on. By the thousands they were also making speeches to groups of all kinds. Many CPAs became recognized as leaders of their communities.

The entry into political life was slower. The lack of partici-

pation by CPAs in their legislatures or in government offices was often contrasted with the extensive participation in public affairs by members of the legal profession. But gradually CPAs began to answer the call, running successfully for election to their state legislatures, and accepting appointments as state auditors or controllers. Many became trustees, and in some cases even mayors, of their villages. A few became mayors of major cities: for example, Norris Poulson served as mayor of Los Angeles and later was elected a member of the U.S. House of Representatives; Frank Wilcox served for many years as mayor of Waco, Texas; and James P. Ould served as mayor of Lynchburg, Virginia, subsequently running unsuccessfully for the United States Senate on the Republican ticket. Christopher Del Sesto, a CPA of Rhode Island, was elected governor of that state.

In the largest city in the country—New York—Abraham Beame, a CPA and a member of the Institute, served for many years as controller and later ran for mayor but was defeated. Herman Badillo, another CPA, became borough president of the Bronx in New York.

William A. Blakley, a CPA of Texas, became a U.S. Senator. Joseph Vigorito, a CPA of Pennsylvania, was elected to the House of Representatives, as was Glenard P. Lipscomb, a licensed public accountant of California, who became chairman of the influential House Committee on Government Operations.

Among the numerous members of the Institute who held important offices in the federal government were Percival F. Brundage, who served as United States Budget Director, and Maurice H. Stans, who served as Deputy Postmaster General, Assistant Budget Director, Budget Director, and Secretary of Commerce.

William B. Franke became Secretary of the Navy, and T. Coleman Andrews and Russell Harrington both served terms as Commissioners of Internal Revenue. Joseph Campbell became Comptroller General of the United States, and Robert M. Trueblood was a member of the President's Commission on

the Federal Budget. Charles A. Boucher served as Assistant Secretary of the Navy, and Neil Harlan as Assistant Secretary of the Air Force.

In 1969 James J. Needham was appointed a member of the Securities and Exchange Commission. A member of the Institute's Council, he was the first CPA to become a member of the Commission directly from public accounting practice: although both Donald Cook and Edward McCormick, former members of the Commission, held CPA certificates, they achieved membership on the Commission through the route of service on its staff.

These are only examples taken at random from a long list of Institute members who held important posts in Washington and in their own states and communities.

The state societies also frequently provided institutional support to their state governments, working with tax commissions and "little Hoover commissions" and in studies of state or city budgets and financial procedures, for which they received public acknowledgment.

At least three CPAs, Lloyd Morey, John Champion, and Charles Johnson served as presidents of great universities.

Thus, it can fairly be said that in the past 30 years members of the accounting profession, in fairly substantial numbers, moved into leadership circles at all levels of society.

The Public Spotlight on Financial Reporting

It gradually became apparent, however, that when the spotlight of public attention again fell on the accounting profession it would focus on what was being done about accounting principles, rather than on auditing standards and procedures, which had been the target following the McKesson & Robbins case.

Earlier chapters of this book describe the mounting criticism of corporate financial reporting which reached its peak in the early 1960's. The demand for comparability of earnings of different companies and, what amounted to the same thing, the denunciation of alternative accounting principles followed in similar circumstances were directed almost entirely at the accounting profession.

To most CPAs this seemed unfair. The SEC, which had the power to compel management to follow whatever rules the Commission adopted, had acquiesced in the gradual, educational approach to improvement adopted by the Institute's committee on accounting procedure—though indeed the Commission had pressed for speedier action and clear-cut decisions. And the committee's work had undeniably resulted in many improvements in corporate financial reports.

All this was ignored by the public in the clamor, stimulated by a somewhat sensational press, following what has been termed the "investment credit fiasco" of 1962-1964. Also ignored were the good work the profession had done in tax legislation and administration, and in federal government accounting; the public-service contributions of individual members; and the improvements in auditing standards and procedures, in accounting education, staff training, and professional development.

Fairly or unfairly, the profession found itself with a public-relations problem of crisis proportions. Something had to be done about it. The investing public was not getting what it wanted, or thought it wanted, and blamed the auditors. The possible responses were to persuade the public that what it wanted, or thought it wanted, was impossible to provide, which was partly true; or persuade the public that the profession could and would provide it, which was also partly true; or abdicate responsibility by turning the whole problem over to the SEC, which no one seemed to advocate.

By rejecting this latter alternative, the Institute implicitly assumed, perhaps more consciously than before, a public-

service obligation of major proportions. It accepted, in full public view, the role of leadership in setting standards of corporate financial reporting. This was the most significant public-service activity the profession had ever undertaken, and the one on which the fate of its public relations largely depended.

Action taken to reassure the public that the profession could do the job has already been described in Chapters 5 and 6. There remained the difficult and delicate task of persuading the public that what it wanted, or thought it wanted—instant comparability of earnings per share—was impossible to provide completely, though many existing obstacles to comparability could in time be eliminated. This was primarily a communications problem—and an extremely difficult one, in which the co-operation of the business and financial press, and of the financial community generally, was essential.

"The Auditors Have Arrived"

Fortuitously, even before the investment credit episode and the consequent barrage of public criticism, the attention of the business and financial press was sharply directed to the accounting profession by an article in *Fortune*.

This article, published in November and December 1960, under the title "The Auditors Have Arrived," was written by Tom Wise, a journalist of superior intelligence and perception, after months of research and countless interviews. He felt, with reason, that he had "scooped" his competitors by discovering an influential element of society which had not yet been carefully examined in print. The article began:

> It is a curious and noteworthy fact that the tremendous growth of the U. S. accounting profession in the postwar years has taken place almost unnoticed by most Americans. In the same years, other proliferating white-collar types—advertising and public-relations men, union and corporation lawyers, stockbrokers, research scientists—have impinged heavily on the national consciousness; news stories about

such men are often in the papers, and their prototypes appear regularly in novels and television dramas. But the rise of the accountants has occurred quietly.

The *Fortune* article was an objective analysis of the profession and its problems—in fact the first fairly thorough analysis by an informed outsider to be published. But its principal focus was on accounting principles—the major public-service area in which the organized profession was engaged. This focus was signaled in one of the opening paragraphs as follows:

> The profession today is fighting a number of quiet but intense battles to clarify and make consistent the accounting principles used in the U.S. It is a truism in the profession, though it still seems a bit shocking to many businessmen, that two different accountants in possession of the same figures may construct two considerably dissimilar balance sheets.

There followed a brief historical review of the profession's origin and development, including the following comment:

> By the time of World War I, the ownership of public securities had become fairly widespread, and there was a growing awareness of the need for more uniformity in financial reporting.

Reference was made to the Institute's collaboration with the New York Stock Exchange in the introduction of financial-reporting standards in the early 1930's.

The expanding tax practice of CPAs, and the "battle with the legal profession" were mentioned (see Chapter 9 herein). Further:

> The "management service" business has burgeoned in the accounting profession during the past few years. Many accountants find it confusing and hard to justify, but others consider it a logical and lucrative extension of what they have been doing in the financial field all along.

Ethical problems, independence, the impact of EDP, and the growing influence of accountants in the federal government

were all discussed. But the main thrust of the article returned to accounting principles.

The second installment began:

> The 71,000 certified public accountants in the U.S. are every year becoming more aware that finding the "right" names for business operations may be the most arduous part of the unending search for a more understandable, more rational, more honest, and more efficient business society. When the terms that measure business performance are used inflexibly, business practices may be unduly constricted. But when these terms are used too loosely, business practice may degenerate into confusion and mistrust. . . .
>
> The Institute has been aware for several years that it will have to take a position either for continued flexibility in handling financial statements or for uniformity.

Referring to the critical speeches of Leonard Spacek, the article said that he "has fought within the profession for rules that would make the financial statements of different companies more readily comparable. Some accountants think his position is too rigid. . . ."

The organization of the Accounting Principles Board in 1959, as a result of Alvin Jennings' 1957 speech, was described, but the author added perceptively:

> It is clear that the profession's principal unresolved problems will have to be solved, ultimately, by the AICPA and its new Accounting Principles Board. It is also clear that the actual powers of the Institute and the Board are still undefined.

In conclusion, Mr. Wise wrote:

> If accountants need some clarification of their powers, they also need a greater public awareness of where that power and responsibility end. Many businessmen are surprised to learn that a corporate financial statement is the responsibility of management, not of the auditing firm. . . . Technically, and legally, the auditor is responsible only for the honesty of his own opinion certificate, in which he ordinarily says that his investigations have led him to believe that the company's assets, liabilities, and earnings reports are fairly presented. . . .

> The selection of independent auditors is more often being submitted for stockholder approval. Some auditors believe that the time may soon come when U.S. stockholders will have the same legal rights as British stockholders, who are entitled, at annual meetings, to have both the old and new auditing firms present when there is any change in auditors. One way or another, it seems likely that auditors in the U.S. will be answering a lot of questions in the next few years.

No one could deny the accuracy of the final sentence.

Mr. Wise predicted that publication of this article in his own prestigious magazine would lead to an increasing interest in the accounting profession on the part of other editors and writers. In this he was correct. The article was, in fact, a basic primer for journalists, and it may be safely assumed that it has been consulted by many writers as they later explored one phase or another of the profession's problems in greater depth.

Unfortunately, perhaps, the profession had no sooner obtained this heightened visibility than the internal controversy about the investment credit provided the journalists with rich material for critical articles—and they made the most of it. Unhappily, most of them were neither as well informed nor as objective as Tom Wise. And so the profession writhed under slashing attacks in *The Wall Street Journal, Business Week, Barron's, Forbes, Harvard Business Review,* and many other publications. Quotations from some of these articles appear in Chapters 5 and 6.

Improving Communications

It was clear that a severe communications gap had existed without the profession's knowing it. Many of the financial writers were clearly unaware of the nature of accounting, the inescapable input of judgment and estimate in periodic financial reporting, the responsibilities of auditors, and the limited ex-

tent to which comparability in reporting earnings per share for a single year was attainable.

For decades CPAs had been clamoring for a public-relations program which would call attention to themselves. Now they were reading more and enjoying it less.

Countervailing action was necessary. It was obviously impossible to respond directly to each of the published criticisms appearing in newspapers and magazines throughout the country. It was decided instead to follow what the staff termed the "displacement theory" of public relations—to emphasize the affirmative rather than going on the defensive. Strenuous efforts were made, with gratifying success, to publicize the action of the Council requiring disclosure of departures from APB Opinions. Press conferences were held on the successive Opinions of the Accounting Principles Board issued after 1964, such as the widely praised Opinions on pensions and net income, and favorable publicity resulted.

A series of seminars for financial editors and writers was undertaken, to which limited numbers of journalists were invited. These took the form of two-day sessions on financial-reporting problems. CPAs made brief introductory statements, which were followed by informal discussion, questions and answers, with "no holds barred." Such seminars were held in New York, Chicago, San Francisco, Kansas City, Dallas, and Atlanta, with a second session in New York in 1969. Most of the important newspapers and financial and business magazines were represented at one or more of these seminars. The results were salutary, and the seminars were expected to continue.

Each of these meetings was followed by generally favorable articles in the publications of the region, giving credit to the profession for what was being done to improve corporate financial statements. Furthermore, the personal acquaintances formed at the financial-writers' seminars led to improved communications later, when APB Opinions or other Institute actions were released for press comment.

The appointment in 1967 of Leonard Savoie, an experienced

CPA, as executive vice president of the Institute, with authority to act as its spokesman, also greatly improved relations with financial writers and editors. He took an active part in the seminars occurring after his appointment. The press learned to have confidence in his objectivity and turned to him for explanations of accounting questions involved in news items or articles.

Public-Relations Policy and Program

The Institute had learned that public relations was an elusive concept, involving action, attitude, and good communications. It had also learned that allocation of scarce resources to communications with various groups—and the measurement of benefits in relation to cost—were matters of great complexity. It had experimented with a wide variety of approaches, at varying levels of sophistication, in relations with many different audiences.

Through the years, from time to time, the public-relations activities had been re-examined, reassessed, and redesigned. Finally, in 1967, the planning committee issued a comprehensive statement of policy and program which, with the approval of the executive committee, was distributed for the information of all members.

The object was to establish public relations as one of the Institute's most important functions, which the membership strongly desired, and to provide a frame of reference for activities in this field.

The assumptions were stated as follows:

> . . . The material of public-relations work (ideas) is subjective. The product (opinion) is intangible. And attainment of the goal (change in attitudes) is difficult to predict and impossible to measure exactly even after the event. So it is little wonder that, in the name of public relations, activities are often undertaken which are so vaguely defined

as to be useless as a guide to planning or as a standard against which to measure performance. . . .

The purpose of public relations is to gain the support of the public, or of significant segments of it, so that an organization can achieve its objectives most readily and completely. This cannot be done, over the long run, by attempts to "sell" a company, or an association, or anything else, regardless of its merit. It is done by *relating* the entity, whatever it may be, to the public. The relating may require changes in the entity's own attitudes, and since the public is constantly changing both in composition and its concerns, and the entity itself is likely to be changing, the relating is a continuing task.

The position taken in this paper is that public relations involves fundamentally two elements—first, action; second, communication. Stated another way, an organization desiring good public relations must first *deserve* respect and confidence, and then must try to *gain attention* for its work and ideas.

The document listed 15 segments of the public on which the accounting profession should concentrate its communications efforts, including editors and reporters, business executives, investors, security analysts, stock exchanges, investment and commercial bankers, the legal profession, government agencies, legislators, educators, students, and the membership of the profession itself.

The basic objectives of a public-relations program were stated, and means of achieving the objectives by specific activities were broadly outlined.

In writing this program the planning committee was assisted by Stewart Schackne, the Institute's public relations consultant, who had formerly been associated with Earl Newsom, and for some 20 years had headed the public-relations department of the Standard Oil Company (New Jersey). A life-long student of public opinion and a skilled writer, Mr. Schackne brought both a philosophical view and technical expertise to his task.

This planning committee paper was intended to serve as a guide to the Institute's public-relations activities in the years ahead.

The Profession's Attitude

In accepting the presidency of the Institute at the annual meeting in the fall of 1968, Ralph E. Kent defined the problem areas which in his opinion needed the profession's immediate attention. Among them were:

> Our need to identify and meet our broad responsibilities as citizens; our need to recognize and respond to our pressing responsibilities to the disadvantaged; and our need to comprehend and react to changing public expectations—both the expectations of our clients and of the users of financial statements on which we express our professional opinions.

He urged individual members to serve, as opportunity arose, as advisors to their government and to enter government service on a full-time basis for short periods of time. He urged the Institute to participate directly in public policy and public affairs, referring to the useful work of the federal taxation committee and the other committees which had advised Congressional groups and government officials.

He urged individual members and the Institute to provide additional jobs for members of minority groups and to facilitate the entry of disadvantaged youth into the accounting profession itself.

And third, he urged the profession to listen sensitively to the expectations of users of audited financial data and to modify its standards and procedures, if necessary, to meet the public need to the extent possible. He said:

> We must be able to demonstrate—and demonstrate conclusively—that we approach all phases of our work—audit, tax, management advisory services—with objectivity and integrity. We must be able to demonstrate, if necessary, that we do not yield to the wishes of clients who pay our fees in reporting on their financial statements. We must continue to demonstrate our determination to clarify accounting principles and eliminate alternative methods of accounting not justified by differing factual circumstances. In a word, I think we must

> re-examine the position of the accounting profession in our society. We cannot afford the luxury of assuming that what we are doing is automatically right and that our critics are wrong because they do not understand us. We must examine their criticism with detachment and, as good auditors, base our conclusions on hard evidence. In short, we must be responsive to changing public expectations.

These remarks demonstrate the maturity of the profession's approach to its public-relations problems at the end of the sixties.

In 1969 the Institute associated itself actively with efforts to assist minority groups through education and employment in accounting firms. Council adopted a resolution looking to complete integration of the profession. Co-operation was being offered to government and other organizations advancing the cause of "black capitalism."

On another front, an effort was undertaken to assist in devising means of measuring cost-benefit relationships in non-profit enterprises, notably social programs financed by government funds.

The Institute was eager to associate itself with high-level causes in which the skills of its members could be useful.

Continuation on this course showed promise of identifying certified public accountants as a profession of the first rank.

CHAPTER 15

Toward a Viable Tax System

OVER the years few of the activities of the accounting profession attracted as much public attention as its tax recommendations. This part of the profession's work also led to extremely helpful relationships in Congress, in the Treasury Department, in the legal profession, and among business groups interested in taxes.

The focal point of these efforts was the Institute's committee on federal taxation (later the division of taxation), whose prodigious labors from 1937 to the present time defy adequate summary.

This committee became one of the relatively few so-called "senior committees" authorized by the Council to speak for the Institute on matters within its jurisdiction, without clearance with the executive committee or Council. Unlike other senior committees, however—for example, the committees on accounting and auditing procedure—the tax committee was not primarily concerned with matters directly related to the technique of accounting practice, or with technical standards,

but rather with the impact of tax law and administration on the business community and the economy in general. In later years, as pointed out elsewhere, the scope of the committee's work was expanded to include development of standards of responsibility and competence in tax practice. But for the most part, its work can fairly be described as public-service activity.

Readers of Volume I of this history may recall that the accounting profession had a large part in making the corporation excise tax of 1909 practicable of application. CPAs also played an influential role in the drafting and administration of the first income-tax law in 1913.

As the law and regulations became more complex, as tax rates rose, as wartime excess-profits-tax measures were enacted, the Institute's tax committee gradually expanded the scope of its concern to include almost every tax bill introduced in Congress, every regulation issued by the Treasury Department, and every phase of administrative procedure adopted by the Bureau of Internal Revenue. From 1937 onward, hardly a year passed without testimony by Institute representatives before Congressional committees; informal conferences with the staff or members of the Joint Committee on Internal Revenue Taxation, or officials of the Treasury and Bureau of Internal Revenue; and the submission of written recommendations on pending legislation or regulations.

Consequently, the size of the tax committee was gradually increased so that the workload could be divided. First it was a three-man committee. In 1937 it was a five-man committee. By 1939 it had been expanded to eight members. In 1944 it was enlarged and reorganized, dividing itself into a subcommittee on current legislation and another subcommittee on research. Five years later it was again reorganized. The office of vice chairman was created, and the membership was divided into three subcommittees: one on current legislation, one on administration, and one on long-range tax policies. At this time also the committee's first full-time staff assistant was engaged.

In 1953 the committee was enlarged to 30, and an executive group was created to co-ordinate the work of the subcommittees. Four years later the committee was again enlarged, this time to 50, and six subcommittees were created to deal with major subject areas, instead of having one group deal with legislation, another with administration, and another with long-range tax policy. Thenceforth each subcommittee dealt with all three aspects of the subject matter within its jurisdiction. The Institute's tax staff was also improved in quality and enlarged in number. Later the number of members of the tax "division" reached 87, with an executive group supervising 12 related committees.

A book could be written about the specific issues on which the tax committee has spoken, and the reasoning underlying its recommendations. Space limitations prohibit any such effort here, but a few examples of its work may illustrate the scope and intensity of its activity.

Extensions for Filing Returns

A perennial subject of concern was the effort to obtain extensions of time for filing tax returns. The burden on taxpayers and their advisors between the close of the fiscal year and the required filing date was often almost insupportable. Bureau of Internal Revenue officials, however, were naturally reluctant to defer collection of the revenues by granting extensions too generously. When basic changes in the tax law were made, the problem of compliance by the time the next returns were due further complicated the problems. Countless hours were spent in correspondence and consultation with the Treasury and Internal Revenue officials, with varying degrees of success, in efforts to obtain extensions of time for filing. Eventually the Institute succeeded in having the filing date for individuals changed to three and one-half months after the close of the taxpayer's fiscal year, which to some extent alleviated the burden. These efforts may be regarded as an exception to the statement that

the committee's concern was not principally with matters affecting the members' practice, although even here an element of public service was involved.

For a Non-Partisan Tax Commission

One of the more dramatic efforts of the committee, which attracted nationwide publicity, was a proposal first made in 1939 that a qualified non-partisan commission be created to determine a permanent policy of federal taxation. This proposal was stimulated by Colonel Robert H. Montgomery, who in his later years concerned himself exclusively with tax practice. He urged that such a commission could create a tax structure within which rates could be raised or lowered as revenue needs indicated, but without continuous changing of the underlying concepts on which taxable income was determined.

This recommendation received official recognition when Representative Treadway introduced a joint resolution in Congress providing for the creation of such a commission. No action on this bill was taken, however. In 1943 the Institute, at its annual meeting, adopted a resolution including the following:

> . . . annual revisions of the tax laws have resulted in the creation of a very complex tax structure which is highly detrimental to the prosperity of the country and . . . the permanent establishment of sound principles of taxation is urgently required to give taxpayers the necessary confidence to face the future;
>
> *Be It Resolved,* That the American Institute of Accountants urges that Congress establish as soon as possible a qualified non-partisan commission composed of members of Congress, representatives of the Treasury Department, independent lawyers, accountants, and economists, to write a simple revenue law which will express a permanent and consistent policy of federal taxation.

Press releases on this resolution were issued, and special mailings were made to state societies, members of the House Ways

and Means Committee, the Senate Finance Committee, the Treasury Department, and the Bureau of Internal Revenue. Favorable editorial comment appeared in the public press, and many government officials expressed sympathetic interest. Fifteen state societies and five of their chapters adopted similar resolutions. Talks made by Institute representatives were released to the press, and the proposal was brought to the attention of business and professional organizations. Editorial comment in *The Journal of Accountancy* kept the subject alive.

In 1944 Representative (later Senator) Frank Carlson introduced a bill embodying the Institute's recommendations, and a campaign was launched to get action on it. Personal interviews with Congressional representatives were undertaken on a large scale. Every effort was made to enlist the support of organizations interested in taxes, the state societies, and the general public. Representative Carlson appeared at a meeting of the Institute's Council to discuss plans and progress.

Two hundred editors of daily newspapers received copies of the bill, together with the Institute's resolution, which resulted in further publicity on the proposed non-partisan tax commission. The proposal was discussed before local chambers of commerce and Kiwanis and Rotary clubs. The president of the Institute wrote to 16 organizations, including banking, credit, business, accounting, legal, labor, farming, and tax research groups, explaining the project and urging them to support the objective. This letter was followed by conferences and luncheon meetings with executives and other representatives of these organizations.

The National Association of Cost Accountants, the National Association of Credit Men, the American Bar Association, and the New York State Chamber of Commerce formally endorsed the idea of a non-partisan tax commission and issued publicity on the subject. The American Bankers Association and the Tax Foundation expressed sympathy with the idea and gave it publicity.

Sixty-nine senators from 36 states, and 165 representatives

from 38 states heard from constituents about the Carlson Bill. Twenty-one state societies took an active part in this effort. Institute representatives, during a six-month period, had 17 personal conferences on the proposal with members of the House Ways and Means Committee and the Senate Finance Committee, and with the Chief of Staff of the Joint Committee on Internal Revenue Taxation.

In spite of all these efforts nothing happened. It seemed clear that in the last analysis Congress would be extremely reluctant to delegate to any outside group even the authority to initiate recommendations, with the official status which a federal law establishing such a commission would give them. But the several years of hard work made Congress more aware of dissatisfaction with the tax system and, incidentally, more aware of the Institute's growing influence in this field. The tax committee concluded that the support which the project had enlisted was indirectly influential in focusing the attention of the House Ways and Means Committee on the need to improve the Internal Revenue Code.

The campaign for a non-partisan tax commission also made the business public more aware of the accounting profession's leadership role in tax legislation. It was also noted in the press that the Institute's efforts on behalf of tax simplification were obviously contrary to the immediate selfish interest of certified public accountants, since the more complicated the law became the more their services would be needed. One observer was reminded of the classic definition of news—"man bites dog."

Tax Accounting and Business Accounting

The subject of conformity of tax accounting rules with accounting principles followed in the determination of income for other purposes was another major issue. In 1945 the tax committee reported to the Council as follows:

> The committee has adopted, as one of its primary projects, a complete study of accounting for tax purposes, with a view to recommending legislation and administrative action which will eliminate, or at least greatly reduce, the increasingly wide gap between generally accepted accounting principles and accounting procedures recognized for tax purposes by rulings and court decisions, which has manifested itself particularly in such matters as prepaid income, deductions for accrued taxes and reserves.

In 1950 the Council of the Institute adopted another resolution, renewing the proposal of a non-partisan commission, but also pointing out that variations between the tax law and generally accepted accounting principles caused unnecessary added expense and uncertainties about tax liabilities; and that piecemeal amendments of the Internal Revenue Code and Treasury regulations, together with varying interpretations by the courts, had resulted in inequities and hardships for taxpayers.

In 1952 a Republican administration was elected for the first time in many years, and a Republican, Congressman Reed, became chairman of the House Ways and Means Committee. The Institute's recommendations received a sympathetic ear. The tax committee reported as follows in 1953:

> The Institute has urged for many years the creation of a non-partisan tax commission which would study the Internal Revenue Code and make recommendations leading to its complete overhaul. The present patchwork technique of modifying the Code from year to year has produced a monster law, filled with inequities and inconsistencies. The new administration has already stated its desire to sponsor such a comprehensive revision of our tax structure and steps have already been taken to initiate partial revision. Congressman Reed has indicated an interest in our proposal for a non-partisan tax commission, and the suggestions of your committee are now being solicited so that an appropriate bill may be formulated for the consideration of Congress.

The report also said that Congressman Reed was sympathetic to reconciliation of tax accounting and business ac-

counting. Referring to a meeting with him, the report said:

> He acknowledged and stressed the necessity for tax accounting to conform to generally accepted accounting principles. At his invitation the Institute is preparing a comprehensive statement enumerating those instances in the Code where the required accounting treatment has deviated from traditional accounting precepts. This matter is more fully discussed also in the report of the executive committee.

The executive committee had authorized the appointment of a special committee, consisting of four members of the committee on accounting procedure and three members of the committee on federal taxation, to attempt, "in response to a request from the chairman of the House Ways and Means Committee," to draft recommendations which would reduce present deviations in tax accounting from generally accepted accounting principles.

This special committee labored diligently, and within a comparatively short time produced a report which was sufficiently persuasive to result in amendment of the Code—though over some opposition from the Treasury Department—permitting recognition of expense reserves as current deductions for tax purposes, and deferring tax on prepaid income until the related goods or services had been provided. These provisions were hailed as a long step toward reconciliation of tax accounting with generally accepted accounting principles.

Almost immediately, however, the Secretary of the Treasury requested repeal of these provisions on the ground that the revenue was adversely affected. Furthermore, the Treasury correctly stated that many corporations, while taking advantage of the new provisions for tax purposes, were not booking the expense reserves in the same manner or including them as deductions from income in reports to stockholders.

As a matter of fact, the fertile imagination of taxpayers, sometimes allegedly abetted by accountants, created new kinds of reserves that had never before appeared in financial statements. The Treasury feared that an escape hatch had

been opened which might result in a loss of current revenue as great as $5 billion.

The chairman of the tax committee discussed the problem at a special session of the Council and was authorized to recommend to Congress that the benefits of current deductions of expense reserves be spread over a ten-year period—as an alternative to repeal of the basic provision. The chairman made this proposal at hearings before the Senate Finance Committee and the House Ways and Means Committee.

Other strenuous efforts were made to prevent repeal of the basic provision. With the co-operation of accounting firms, statistics were independently gathered, which indicated that the impact of these provisions on the revenue would be not nearly as great as the Treasury feared. Sessions were held with the Joint Committee on Internal Revenue Taxation to argue for their retention. Representatives of 15 different organizations were called to a meeting by the Institute to discuss the matter, and were urged to add their voices to the appeal to retain the basic principle.

However, by that time the die was cast. Both the Congressional committees voted unanimously to repeal the controversial provisions, and they were repealed outright in 1955.

The outlook for reconciliation of tax accounting rules with accounting principles used for the determination of business income was bleak. The decision of the United States Supreme Court in the *Schlude* case in 1963 was another blow. Despite *amicus* briefs filed by the Institute in both the Court of Appeals and the Supreme Court, it was held in that case that prepaid income was taxable in the year received, although the related services were to be rendered largely in subsequent years. This decision met with outraged indignation throughout the accounting profession and the business community.

The disparity between tax accounting and business accounting continued to disturb the Institute's tax committee, and in the following years it continued to recommend a return to the basic principles adopted in the 1954 amendments, with adequate safeguards.

Technical Tax Advice

These unsuccessful efforts at broad-scale reform of the tax structure, however, by no means constituted the major contribution of the tax committee. Most of its work was concerned with technical aspects of tax law and with the regulations and administrative procedures involved in its enforcement. It is in these areas, where year after year hundreds of recommendations have been submitted, that the cumulative impact of the committee's work was most remarkable. It helped the Treasury and the Internal Revenue Service to develop a viable tax machinery, and it eliminated inequities, many of them unintentional, which might have crept into the laws and regulations.

For example, when the wartime excess-profits-tax law was proposed in 1940, the Institute's tax committee submitted to the Joint Committee on Internal Revenue Taxation a 33-page memorandum based on intensive study of the proposals. Of 13 specific recommendations contained in that memorandum, seven were adopted in full, one was adopted in part, and five were not adopted by the subcommittee of the House Ways and Means Committee. Subsequently, however, three of these five were partially adopted in either the House or Senate versions of the bill. When the legislation was actually formulated, six new recommendations were made by the Institute's committee: three were adopted in full, one in part, and two rejected, one of which was later adopted by the Senate. In summary, 31 specific recommendations were made, 18 of which were adopted in full, four in part, and nine were not adopted, five of which were described as of little consequence and two of limited importance. The accounting profession had a significant influence on the form of that legislation.

The committee also assisted the Treasury Department in developing the excess-profits-tax return form and in developing regulations dealing with accounting problems, the relief sections, and consolidated returns.

In later years, the committee was influential in mitigating the impact of the double tax on corporate income, and in removal of the 2 per cent penalty on the filing of consolidated returns.

Reorganization of the Bureau

In 1952, partly as the result of scandals involving high officials of the Bureau of Internal Revenue, a full-scale reorganization was undertaken, involving decentralization of the tax-collection procedures under regional commissioners, strengthening of the inspection service, a change of the Bureau's name to "Internal Revenue Service," and numerous other features. The Institute's tax committee, while supporting the plan in general, presented specific recommendations on numerous technical questions in oral testimony before the Senate Committee on Expenditures in the Executive Departments. Subsequently meetings were held with the Commissioner of Internal Revenue, T. Coleman Andrews, past president of the Institute and the first CPA to be appointed to this office. At his request confidential comments were submitted related to tax administration and procedures of the Service.

In 1953 the Commissioner created an Advisory Committee, which met frequently to consult with him. Among the membership were two representatives of the Institute, as well as representatives of the American Bar Association and other organizations. This Advisory Committee was continued by subsequent commissioners and has provided an opportunity for informal, frank discussion of problems of tax administration.

In 1954 the tax committee undertook a survey of the membership to determine how the new administrative procedures under the reorganization plan were working out—specifically, in part, to determine whether inconsistencies were developing in applications of the law and regulations in the several

regional districts. The responses to this survey from the membership were analyzed and submitted in a confidential report to the Commissioner himself, who expressed appreciation of this information. Six similar surveys were made in subsequent years, each of which produced more than two thousand responses from practicing members of the Institute, and analyses of these responses were submitted to the Commissioner in confidence.

Tax Legislation and Regulations

In 1952 the tax committee adopted the policy of printing in pamphlet form its recommendations for amendment of the Internal Revenue Code, and of distributing copies widely among members of Congress and other organizations. Copies were also released to the press, which resulted in wide publicity.

In subsequent years, recommendations adopted by Congress were, of course, eliminated from successive editions of the pamphlet, while recommendations not adopted, if considered still to have merit, were repeated periodically. This heightened visibility of the committee's recommendations added to their weight, since public awareness of the Institute's suggestions increased the difficulty of ignoring them without sound reasons.

The 1954 revision of the Code was described by the tax committee as the largest in volume, the greatest in extent of overhaul, and the shortest in amount of time available for consideration ever in the history of the tax laws. The committee held a three-day-and-night session in Washington to study the bill, following which the executive group spent another day in consideration of the proposals. Nine days later the executive group had a four-day-and-night session.

The result of this concentrated effort was 213 recommendations for changes in the proposed Code.

There followed a two-day session with government technicians in review of the proposals and, later, testimony before the Senate Finance Committee.

The report of the chairman of the tax committee to the Council said, "The reaction of the government technicians is noteworthy. Their general view, overtly expressed by some, was that the Institute's presentation was an objective one." Of the 213 recommendations, 105 were adopted. The recommendations were the subject of editorial comment in the public press and were received with interest by other tax groups, including members of the Bar.

Incidentally, in that same year, a tax committee proposal for averaging income for tax purposes attracted much public attention, including favorable comment occupying the entire editorial column of one of the New York papers and an article by a tax columnist in another.

When the 1954 law was enacted, the members of the committee prepared a technical analysis which composed a special issue of *The Journal of Accountancy,* in order that the membership of the Institute might, as quickly as possible, receive a summary of the effects of the new provisions. In addition, members of the committee discussed the effects of the new law with various editors and writers.

In 1957 another major piece of tax legislation was introduced—known as the Technical Amendments Bill. Fifty-two amendments to the Code were proposed. As copies of the bill became available, the government also issued a list of 33 substantive unintended benefits and hardships, with an invitation for suggestions. Most of these problems were controversial in nature.

Again, time was short. Within a few weeks the executive group of the tax committee had to review these proposals. The chairman testified before the Subcommittee on Internal Revenue Taxation on 16 of the 52 sections of the bill, and 14 of the additional 33 problems on which advice had been requested.

At the conclusion of the testimony, Representative Wilbur

D. Mills, chairman of the Congressional subcommittee, made the following remarks:

> The American Institute of Accountants has rendered a valuable public service in the attitude which the organization has taken with respect to improvement of our tax laws, pointing out those things that operate adversely against both government and taxpayer. . . .
>
> You are to be commended upon the very public spirited attitude that you have taken in the past and that you are still taking as accountants. . . .

The tax committee's record in commenting on regulations was equally impressive. In one year, for example, of 125 specific suggestions on proposed regulations, 25 per cent were adopted. In another year, out of 382 suggestions, 33 per cent were adopted.

In addition to its other services, the tax committee, in 1953, undertook a review of the various tax-return forms. In the following year it was requested by the Service to review drafts before changes in the forms were finally adopted. In every subsequent year the committee sought recommendations from the membership on changes in the tax forms, reported to the Internal Revenue Service on these recommendations, and worked with the Service in the application of desirable changes. Each year the results have been a distinct improvement over preceding forms. For this the Institute's committee earned the thanks of successive Commissioners.

Among other things, the committee persuaded the Service to permit duplication and reproduction of tax returns by photographic methods. Previously it had been required that all returns be made on the official forms provided by the Service itself.

Year after year the activities which have been illustrated by examples were continued. No revenue bill, no Treasury regulation, no significant IRS policy, no change in the tax-return forms escaped the Institute's examination.

In 1964 it was suggested that the recommendations of the tax committee on law and regulations would be of interest to

many members engaged in tax practice. Since the volume of this material precluded its publication either in *The Journal of Accountancy* or separately, it was decided that members who wished to subscribe would receive duplicate copies of all the committee's legislative recommendations, comments on regulations, briefs, memoranda, and so forth. More than 2,000 members took advantage of this opportunity.

In 1965 the committee remarked in its report that while the Congress had not responded immediately to the committee's pending suggestions, experience had indicated that sound recommendations had tended to gain acceptance over a period of time, often being incorporated in the tax law years after their original proposal. For example, it was said that the recent introduction of income averaging had followed many years of urging by the Institute's tax committees.

General Policy on Taxation

For many years the recommendations of the tax committee were mainly on technical and administrative matters, rather than suggested tax rates or provisions of special interest to particular industries.

Back in 1941 the committee said:

> We have adopted the principle that our committee, or the Institute through this committee, should not participate actively in lobbying or working for legislative amendments, nor should we take a definite position with respect to amendments intended to benefit particular groups or classes of taxpayers. Your committee is of the opinion that it should confine its activity to submitting to Congress and the Treasury the benefit of our experiences and our opinions with respect to the general application of tax statutes, technical effect of the requirements of the law, and, accordingly, not participate in such efforts as involve benefiting one group or class of taxpayers at the expense of another.
>
> Your committee believes that this policy of acting as disinterested professional advisors, not seeking benefits for themselves or a particular group, contributes much to the weight of our influence.

The line between technical and administrative matters and policy questions, however, was not always easy to distinguish. On occasion the committee was accused of submitting recommendations which would be especially advantageous to business organizations—the clients of certified public accountants. It could be argued in defense that changes favorable to taxpayers through removal of inequities, simplification of procedures, and lightening burdens of compliance would be advantageous to the government by expediting collection of revenues and strengthening taxpayer confidence in the system. On the other hand, it could well have been that the familiarity of CPAs with the impact of taxes on business decisions and business procedures subconsciously imbued them with the business point of view to some extent.

However, the tax committee was always sensitive on this question. On broad policy matters, such as the proposal for a non-partisan commission and the reconciliation of tax accounting with business accounting, the committee asked the Institute's Council or its executive committee to assume ultimate responsibility.

A specific policy question arose in 1951. The committee reported to Council that it had been asked by Congressional representatives to make a recommendation as to whether additional revenue required for prosecution of the Korean war should be raised by an excess-profits tax, by an increase in the existing corporate rate structure, or by other means. It was also asked to express an opinion as to the proper maximum effective rate of tax. Said the report:

> The committee recognized that such a recommendation would, of necessity, have to be the expression of the opinion of the individual members . . . and could not be that of Institute membership at large. The committee, following traditional policy, refrained from making a definite recommendation as to whether an excess-profits tax act should or should not be enacted, and as to the maximum rate, but confined itself to the technical aspects of the proposed legislation. . . .
>
> The committee itself is not yet ready to ask for a definite change in policy. The committee is interested in obtaining the views of the

Council as to whether the practice which has been followed has established a traditional policy which should be followed by the committee until a change has been authorized by the Council.

In response, the Council encouraged the committee to use its own judgment in determining when to venture into what might be called the "policy field." Studies were then undertaken on long-range tax policy, including such topics as averaging of income, corporate taxation, family tax, capital gains and losses, estate and gift taxes, charitable foundations and organizations exempt from tax, depreciation, and similar matters. Papers on some of these subjects were prepared by members of the committee and published in *The Journal of Accountancy.*

However, it was not until 1969 that the question was finally resolved. The Institute's executive committee approved a report of the tax-policy committee of the division of taxation, proposing initiation of a program for developing positions in matters of tax policy covering major areas of taxation in which members of the accounting profession had special competence.

Previously, the report said, the tax committee had "confined the expression of its views. . . to technical matters within the established framework of the tax structure. . . ." The new program, it was said, would permit expression of views on tax policy only on matters in which CPAs as a group had "recognized special competence and experience," only when supported by competent and adequate research, and only when consistent with the goal of a sound and effective tax structure in the public interest.

Drafts of tax-policy statements would be exposed widely for comment before adoption.

Administered with complete objectivity, this new program offered opportunity for even greater constructive contributions by the accounting profession than those of the past.

On the whole, judging by reactions of legislators, and Treasury and Internal Revenue officials, the committee had succeeded in maintaining a reputation for objectivity. For example, in the *Harvard Law Review* of May 1957, Stanley S. Surrey,

later Assistant Secretary of the Treasury for Tax Policy, published an article entitled "The Congress and the Tax Lobbyist —How Special Tax Provisions Get Enacted." In this article he said:

> The Tax Section [of the American Bar Association] . . . has not yet become a vocal ally of the Treasury in defending the integrity of the tax system before the tax committees. In this respect it appears to be lagging behind the other chief professional group in the tax field, the accountants. Over one-third of the items in the 1955 statement of tax proposals of the American Institute of Accountants are recommendations urging the elimination of tax provisions which it considers to constitute unjustified favoritism for special groups. Yet one can scan report after report from the American Bar Association without finding a single similar recommendation.

Other Activities in the Tax Area

As a special public-information effort, the tax committee in 1954 sponsored and organized a tax conference in St. Louis for business executives, which was so successful that it was repeated two years later in New York.

In 1956 the Institute was requested to recruit a CPA of junior partner or managerial rank to serve as a full-time consultant to the Treasury Department in the drafting of tax legislation and regulations. It was suggested that one of the firms might release a man for one year to take on this assignment.

Without hesitation one of the larger firms released one of its best men for this purpose. The experiment was so successful, both from the point of view of the Treasury Department and from that of the individual concerned, who regarded the year's work as a broadening and enriching experience, that it was repeated in subsequent years. Different firms provided a recruit in each of these years.

The CPAs thus temporarily serving in the Treasury's legis-

lative drafting department were consulted on legislation or regulations which had accounting implications, to determine what was sound or practicable in relation to accounting principles and procedures normally followed by business.

In order to improve communications with the staff of the Internal Revenue Service and with the Tax Section of the American Bar Association, representatives of these groups were invited to attend meetings of the enlarged tax committee in the early 1960's. On occasion, the Commissioner himself would attend, accompanied by high officials of the Service. These meetings have become an annual event. In turn, the Tax Section of the Bar Association has invited Institute representatives to meet with its senior groups.

In 1964 the tax committee, after several years of preliminary discussions, undertook the publication of "Statements on Responsibilities in Tax Practice"—guides to certified public accountants in the conduct of their tax practice. This effort was warmly praised by the Commissioner of Internal Revenue and by others. Five statements on responsibilities have been published and others are under consideration, as noted in Chapter 17.

In 1967 a project to produce research studies in federal taxation was undertaken. The objective was to help maintain and improve technical proficiency in taxes on the part of the CPA in general practice and of tax staff personnel. The first of these studies was published in 1969 and others were in process.

The "Tax Clinic," a monthly department in *The Journal of Accountancy* edited by successive members of the tax committee, and later by the director of taxation, was a popular and useful service to the profession. So valuable was much of the material published in the "Clinic" that excerpts were brought together in a brochure published annually under the title *Working With the Revenue Code,* which enjoyed wide circulation.

The latest Institute venture is the publication of a new tax magazine, *The Tax Adviser.* The first issue was published in January 1970.

The contribution which public service can make to public relations is well illustrated by the experience of the Institute's committee on federal taxation. The enormous volume of work accomplished and the hundreds of recommendations submitted have attracted favorable notice in high places and wide publicity over the years. Way back in 1941, the Institute's secretary said in his report to the Council:

> The committee on federal taxation, which has provided an outstanding example of public service by the accounting profession, has contributed much to good public relations.

Twenty-eight years later, that remark could be doubled in spades.[1]

---

[1] In this fragmentary and highly condensed recital, it is impossible to give proper credit to the many individuals who have made substantial contributions to the tax committee's work. Rather than naming only those concerned with the incidents chosen here as examples, it seems preferable to list the successive chairmen during the period covered by this volume—even though this denies fair recognition to subcommittee chairmen and members—as follows:

Victor H. Stempf	1935-1939	Thomas J. Green	1950-1953
Walter A. Cooper	1939-1942	J. S. Seidman	1953-1956
J. A. Phillips	1942-1943	Wallace M. Jensen	1956-1959
George P. Ellis	1943-1944	Leslie Mills	1959-1962
Maurice Austin	1944-1947	Thomas J. Graves	1962-1965
Mark E. Richardson	1947-1950	Donald T. Burns	1965-1968
William T. Barnes	1968-		

In recent years, Gilbert Simonetti, director of taxation, has been largely responsible for the widening scope and high quality of the committee's work.

CHAPTER 16

Improving Government Accounting

A MAJOR opportunity for public service by the accounting profession was in the field of government accounting. Control of government expenditures was essential if taxes were to be kept at tolerable levels. Yet not so many members of the profession were as deeply interested in government accounting as they were in taxation. The former was a highly specialized and somewhat mysterious subject, while taxation was a familiar field in which most CPAs felt at home.

Fortunately there were always a few farsighted CPAs who saw the vital importance of good financial management in government and were willing to give their time and energy to help improve it.

As early as 1906 the Institute's predecessor organization had given helpful advice in a reorganization of the procedures of the several departments of the federal government.

Later, President Taft appointed a certified public accountant, Harvey Chase, to a Commission on Efficiency and Economy, where he vigorously advocated legislation providing for

a federal budget. In this he was strongly supported editorially by *The Journal of Accountancy.* The Budget and Accounting Act of 1921, based on this Commission's recommendations, established the Bureau of the Budget and the General Accounting Office. This was a major forward step, in which the accounting profession had at least a minor part.

In 1937, immediately after the merger of the American Society of Certified Public Accountants with the Institute, George P. Ellis, a former president of the Society, was appointed chairman of a committee on government accounting. Mr. Ellis, a Chicagoan, was a partner of the public accounting firm of Wolf & Company. He had demonstrated keen interest in the financial-management problems of local government units, in the solution of which he felt strongly that the accounting profession could make a substantial contribution. In this belief he was joined by two energetic members of his committee, Lloyd Morey, a member of the Institute and Comptroller of the University of Illinois, and T. Coleman Andrews, then a young Virginian, partner of the Richmond accounting firm, T. Coleman Andrews & Company, who had already distinguished himself by serving as state auditor of Virginia and Comptroller of the City of Richmond. These three men were the spark plugs in the profession's efforts to aid in improving federal government accounting.

However, the first activity of this committee on government accounting was participation in the work of the National Committee on Municipal Accounting, sponsored by the Municipal Finance Officers Association, and including representatives of the American Accounting Association, the American Municipal Association, the International City Managers' Association, the National Association of Cost Accountants, the National Association of State Auditors, Comptrollers and Treasurers, and the National Municipal League, as well as the Institute.

The National Committee produced manuals on accounting, auditing, financial reporting, and fiscal controls for municipalities. These useful publications were influential throughout the United States, and in other countries as well. The Institute

representatives were able to make helpful contributions to this work, but soon concluded that the CPA profession should be even more strongly identified with the problems of government accounting.

The Conference on Municipal Accounting

At the committee's initiative, the Institute sponsored a two-day conference in Chicago in 1938, on municipal accounting and financial reporting. To this conference were invited not only practicing CPAs but also public officials, investment bankers, and surety company representatives, all of whom had a strong interest in the financial information available from municipalities.

As a special event at the conference, one speaker from the federal government was invited to tell the assembled audience how accounting was conducted in Washington. The speaker was E. F. Bartelt, Commissioner of Accounts and Deposits of the United States Treasury Department. His speech excited the interest of the Institute's committee in the problems of federal government accounting.

The 1938 conference on municipal accounting was a public-relations coup. The proceedings were published and were widely distributed among interested groups. The reactions were highly encouraging. Thereafter the Institute's committee continued full participation in the work of the National Committee on Municipal Accounting, but its major interest gradually swung over to federal government accounting. Its 1939 report to the Council said:

> In view of the growing importance of, and interest in, accounting problems of the federal government, a special subcommittee was appointed to deal particularly with this matter. . . . A brief statement concerning this problem was prepared and published in the February issue of *The Certified Public Accountant*. . . . A letter was addressed to 16 persons having responsibility of a major character in various

divisions of the government for accounting and fiscal procedure. The letter gave information concerning the committee and the special subcommittee, and offered to aid to the extent possible. A number of these letters were courteously acknowledged indicating an appreciation of our interest in the problem. E. F. Bartelt, Commissioner of Accounts and Deposits, has submitted various material to members of the committee for comment.

The statement in *The Certified Public Accountant,* to which reference was made, was signed by Lloyd Morey, then chairman of the committee, and said in part:

> The problem of accounting of the United States Government, both as to organization and as to procedure, is one of the greatest problems of the kind in the world. Its difficulties are enhanced by the complexities of federal organization, the wide diversity and location of activities, and the numerous laws governing it. The problem is one which should enlist the interest of all accountants, both as citizens and as experts. . . .
>
> Some persons feel that, although the General Accounting Office has failed to achieve the results expected of it and many deficiencies prevail, the organization in principle is correct and existing difficulties can be overcome. Others, however, favor a separation of accounting and auditing in the manner followed in most private business organizations. Some would favor the centralization of accounting in a financial department of the executive division of the government, while others would favor as large a decentralization as possible so that accounts would be attached to and kept in accordance with the need of the various departments and activities.
>
> Whatever may be said for the different opinions, it is clear that the problem is primarily one of accounting and should be settled in accordance with sound accounting principles. For that reason it is fitting that the American Institute of Accountants should take an active part in its consideration. . . .

In the following year the special subcommittee conferred with several important fiscal officials of the federal government and responded to their requests for a memorandum of comments and suggestions. The committee reported:

It is believed that in due time opportunity will be presented for the Institute to render constructive service in this important field. The aim of the committee has been to keep the discussion on a plane of fundamental principles and to avoid being drawn into problems involving internal relationships or partisan political considerations.

. . . The President has issued an executive order directing the Treasury Department to set up a central system of summary accounts and to compile when requested a complete, consolidated report of the government as a whole. . . . This order represents a definite forward step . . . and should result in overcoming many of the deficiencies pointed out by our committee. . . . While the committee was not consulted as to this particular order, it is reasonable to assume that our recommendations and comments had considerable influence in bringing it about and in its scope.

The more the Institute committee learned about federal government accounting and auditing, the more opportunities for improvement appeared. Sweeping reforms appeared desirable to modernize the government's approach. However, the government did not seem eager to be reformed. The committee reported in 1941:

Several efforts have been made to contact the newly appointed Comptroller General, Honorable Lindsay C. Warren, who took office on November 1, 1940, for the purpose of securing his interest in recommendations of the committee affecting his office. Unfortunately no success has attended these efforts. Contacts with some of the members of his staff have not produced any evident effect and have indicated a considerable lack of understanding of the principles which the committee has endeavored to emphasize, and of proper methods of auditing and of financial reporting.

The report went on to praise the Treasury Department for its efforts to carry out the President's executive order for a centralized system of accounting. References were also made to a report of the Brookings Institution on the federal financial system, as requested by the Senate Select Committee to Investigate the Executive Agencies of the Government. H. P. Seidemann, a CPA and a member of the staff of the Brook-

ings Institution, had been added to the Institute's committee.

In the fall of 1941 this committee reported:

> In view of the slowness of progress toward the objectives set by our committee, and in view of the steadily increasing importance of all phases of federal finance to all citizens, the time probably has come for the Institute to enter into a wider discussion and possibly take a more positive stand on matters of federal organization and administration with respect to which it is qualified to speak with authority as a professional body.

The Conference on Federal Government Accounting

What the committee had in mind was a national conference on federal government accounting similar to the highly successful conference on municipal accounting held in Chicago in 1938.

The committee persuaded the Treasury Department, the General Accounting Office, and the Bureau of the Budget, to co-operate with the Institute in a conference on federal government accounting. It was held in New York, December 2 and 3, 1943, and its impact was unmistakable. In addition to the Treasury, GAO and Budget, many other federal government agencies were represented by accounting officials, and a number of practicing certified public accountants were present.

George Ellis was general chairman. Lloyd Morey made the opening address. Papers were presented by J. Weldon Jones, CPA and member of the Institute, who was assistant director in charge of the Fiscal Division, Bureau of the Budget; by Mr. Bartelt of the Treasury Department, with whom the committee had developed cordial relations dating back to 1936; by R. H. Slaughter and J. Darlington Denit, both

of the General Accounting Office; by Eric Kohler, CPA and Executive Officer, Petroleum Administration for War (previously Controller of TVA); and by William R. Quigley, chief of the Division of Accounting of the Department of Agriculture.

Following the formal papers there was extended general discussion, in which the General Accounting Office representatives found themselves frequently on the defensive. Objections were voiced to the GAO's legalistic pre-audit procedure, involving the shipping of vouchers and supporting documents to Washington, and the open-ended liabilities imposed on certifying and disbursing officers until payments had been approved; to the general absence of accrual accounting; to the lack of financial audits, of the kind common in industry, even of business-type operations of the government; to the absence of co-ordination and consistency in the requirements of the General Accounting Office, the Treasury Department and the Bureau of the Budget; and to the fact that the GAO made administrative determinations and then audited payments which it had already determined could properly be made.

The proceedings of the conference, including a full transcript of the general discussion, were published and were widely distributed. This document provided food for thought in Washington.

It had been brought out in the discussion that representatives of the GAO, the Treasury, and the Budget Bureau were having informal luncheons to discuss their common problems. In his final summary, Chairman Ellis suggested creation of a joint committee to develop constructive proposals. He offered the assistance of the Institute, and said, "We have no motives other than to make a contribution to our government, and we think that the accounting profession is a group of men who know, if anyone does, something about accounting and auditing. We have been eager to give our government the benefit of this fine body of talent, but it has been most difficult to know where to start."

Soon after, however, attention was diverted from the subject of governmental accounting in general, to the specific problem of financial control of the so-called government corporations—business-type enterprises, such as the Tennessee Valley Authority and the Reconstruction Finance Corporation, created by the government, but operating on a quasi-independent basis.

There had been expressions of growing concern on the part of the public and the Congress over the increasing number of such government corporations, and the need for independent audit of their operations. The Congressional Joint Committee on Reduction of Non-Essential Federal Expenditures had undertaken a two-year study of the problem, with staff assistance from the Treasury, Budget, and General Accounting Office. This resulted in a report in August 1944, recommending legislation providing for business-type budgets, accounting control, and audit of such corporations by the GAO.

In the same year the Citizens National Committee released a study indicating that the annual expenditures of government corporations aggregated billions of dollars a year; of these corporations only nine were audited by the General Accounting Office, and ten by independent professional accountants, while 32 were not audited at all.

At about this time a Senate committee eliminated an appropriation for independent audit of the Tennessee Valley Authority by certified public accountants, on the ground that the TVA was already audited by the General Accounting Office and the independent audit was a useless duplication. In the hearings, misunderstanding was evident as to the nature of the independent audit of financial statements as contrasted with the GAO's audit to determine the legality of payments. The chairman of the Institute's committee on government accounting submitted a statement to interested senators,

which was incorporated in the record of the hearings, and the proposed amendment which would have eliminated the appropriation for an independent audit was dropped. The appropriation remained and was enacted into law.

On December 20, 1944, the chairman of the Institute's committee on government accounting received a letter from Senator Harry F. Byrd requesting the Institute to form an unofficial committee with representatives of the principal government bodies to consider problems of control, audit, and financial-reporting mechanisms for the federal government corporations, and also the broader subject of accounting and auditing for the federal government as a whole.

An unofficial committee was formed, including representatives of the Institute, the Treasury Department, the Budget Bureau, the GAO, the Foreign Economic Administration, the Department of Agriculture, the Reconstruction Finance Corporation, and the Brookings Institution.

The committee met in February 1945, and appointed three subcommittees, one on budgeting and accounting classification, another on basic legislation, and a third on control of federal corporations.

In this same month, however, Congress responded to the recommendations of the Joint Committee on Reduction of Non-essential Federal Expenditures by enacting a law (Public Law 4, 79th Congress) providing, among other things, that the financial transactions of all government corporations be audited by the General Accounting Office "in accordance with principles and procedures applicable to commercial corporate transactions."

Even broader controls were provided soon after in Public Law 248, 79th Congress, known as the Government Corporation Control Act. This legislation also required audits of all wholly owned government corporations and mixed-ownership government corporations by the General Accounting Office "in accordance with the principles and procedures applicable to commercial corporate transactions." In addition, wholly owned corporations were required to submit a budget pro-

gram to the Bureau of the Budget in the form of a "business-type budget, or plan of operations, with due allowance given to the need for flexibility, including provision for emergencies and contingencies, in order that the corporation may properly carry out its activities as authorized by law."

A provision was included to permit the Comptroller General to engage the professional services of firms and organizations for temporary periods or for special purposes in the conduct of the audits of government corporations.

While this legislation was under consideration, representatives of the Institute were in close touch with Lindsay Warren, the Comptroller General, who was a member of the Bar and a former member of Congress, and with the Assistant Comptroller General, Frank L. Yates, also a member of the Bar.

In April 1945, Messrs. Seidemann and Ellis testified on behalf of the Institute at hearings on the Government Corporation Control Bill before a subcommittee of the Senate Committee on Banking and Currency. They supported the legislation strongly, while offering a number of specific recommendations.

This law was enacted December 6, 1945. Upon enactment of Public Law 4 in February 1945, the Comptroller General had announced his intention of building up a new division to conduct commercial-type audits of the federal corporations. Having become well acquainted with Institute officials, he invited their advice. The result was an appearance before the Council of the Institute early in May 1945, where the Comptroller General asked for the assistance of the Institute in staffing this new division.

The leaders of the Institute recommended T. Coleman Andrews as the best man available to head up the new division. Arrangements were made to recall him from active duty as a Captain in the Marine Corps, where he had served since 1942, in order to permit him to take over this important new post. The war was virtually over, and it had been his intention to return to the public practice of accounting. How-

ever, Mr. Andrews was persuaded of the enormous importance of the position he was being offered. He yielded his personal preferences to the call for public service, and accepted appointment as Director of Corporation Audits in the General Accounting Office. Appointed as Deputy Director of the Corporation Audits Division was Howard W. Bordner, also a CPA and a member of the Institute. An Institute committee was immediately appointed to assist Mr. Andrews in a consulting capacity in the development of technical procedures.

The secretary of the Institute worked with the Assistant Comptroller General in a co-operative effort to secure accountants experienced in the conduct of independent audits to staff the new Corporate Audits Division of the GAO.

In his report for the fiscal year ended June 30, 1945, the Comptroller General said:

> An outstanding milestone in the federal government's financial system was reached when the Congress enacted Section 5 of the Act of February 24, 1945. . . . The importance of this audit duty is shown by the fact that on March 1, 1945, government corporations had total assets of $29.6 billion and total liabilities of $28.4 billion, including intercorporate items.
>
> The audit provisions of the above section are restated with certain clarifications in S. 469 and H. R. 3660 [the bill on which Institute representatives testified], providing further financial control of government corporations. . . . I feel that such legislation represents the most forward looking and outstanding measure in its field since the enactment of the Budget and Accounting Act in 1921.
>
> A new Corporation Audits Division has been set up within the General Accounting Office, headed by a certified public accountant of long experience. The public accounting profession is co-operating splendidly in our efforts to build the finest aggregation of accounting talent within or without the government. I sincerely believe that with this staff and the special resources available, the General Accounting Office will be better equipped than any private accounting firm to conduct the audits of government operations. . . .

The Comptroller General was naturally proud of his own organization and reacted somewhat defensively to suggestions

that accounting firms might be engaged by GAO to conduct some of the required audits. Yet his report for 1946 shows that public accounting firms, by arrangement with GAO, audited 51 corporations of the Farm Credit Administration, 12 District Federal Home Loan Banks, the Home Owners Loan Corporation and the Federal Public Housing Authority.

Origin of the Joint Program

The Institute committee had continually proposed that the accounting and auditing functions of the government should be separated, instead of both being under the control of the GAO. This proposal had apparently been approved by the informal joint committee of government and Institute representatives, created by Senator Byrd's request of December 1944, which submitted a preliminary report to Senator Byrd in April 1946. The Comptroller General, again not unnaturally, strongly resisted this idea.

In the same month the Institute committee reported to the Council:

> We have been unofficially advised that the reaction of the Comptroller General to this report was not at all favorable. . . . Considerable difference of opinion has arisen on the matter of what divisions of government should take over the administrative accounting activities if they are to be removed from the General Accounting Office. Representatives of the Treasury Department seem to think that they should be the agency to assume this responsibility, whereas the Bureau of the Budget suggests that certain control features should be delegated to their Bureau. It is planned to have a meeting of the representatives of the government groups for the purpose of ironing out some of these differences of opinion.

This issue, among others, was soon transferred to the agenda of the Hoover Commission.

Meanwhile, the provisions for audit of government corporations "in accordance with the principles and procedures appli-

cable to commercial corporate transactions" became a model, and the Corporation Audits Division of GAO became a nucleus for a comprehensive, decentralized program for audits of the regular government agencies, which was initiated by the Comptroller General in 1949.

Rapid progress was being made.

However, the need for a thorough study of the accounting and reporting systems of the federal government as a whole was becoming apparent. Representatives of the Comptroller General, the Secretary of the Treasury, and the Director of the Bureau of the Budget got together alone to discuss the best approach to the problem. It was agreed that a co-operative improvement program would be undertaken as a joint venture by these three agencies.

This was the beginning of the joint program for improving accounting in the federal government, which was officially announced to the heads of departments and agencies by the Comptroller General on October 20, 1948. Known as the Joint Financial Management Improvement Program, this project became a permanent, continuing activity of the three agencies, with the objective of co-ordinating budgeting, accounting, reporting, auditing, and other financial-management functions in the operations of the government.

The joint program was endorsed by the Congress in a declaration of policy contained in the Budget and Accounting Procedures Act of 1950, in which it was stated, "It is the policy of the Congress in enacting this part that. . . the Comptroller General of the United States, the Secretary of the Treasury, and the Director of the Bureau of the Budget conduct a continuous program for the improvement of accounting and financial reporting in the government."

After organizing the new Corporation Audits Division of the GAO and putting it on a working basis, T. Coleman Andrews resigned as director and returned to the public practice of accounting in Richmond. He was succeeded by Stephen B. Ives, also a CPA and a member of the Institute.

Hoover Commission Proposals

Mr. Andrews was immediately appointed chairman of a newly created committee on federal government accounting of the Institute. In his first report on behalf of that committee, he stated that he had been asked by former President Herbert Hoover, chairman of the so-called "Hoover Commission"—the Commission on Organization of the Executive Branch of the Government, created in 1947—to undertake the development of an appropriate plan of accounting, auditing, and financial reporting for the government.

This task was undertaken by the Institute's committee on federal government accounting. Staff assistants were provided by the Hoover Commission, and the following top-level government officials were appointed as an advisory group to the Institute committee: Walter F. Frese of the GAO; the Institute's old friend, Edward F. Bartelt of the Treasury Department; and Frederick J. Lawton of the Budget Bureau.

Significantly, Mr. Frese was the man who for several years pulled the laboring oar in the Joint Financial Management Improvement Program. He later became a professor of accounting at the Harvard Graduate School of Business Administration, and for three years served as a member of the Institute's Accounting Principles Board.

During the next few years the focus of the Institute's efforts in the area of government accounting was on the Hoover Commission. Institute representatives testified before Congress in support of some of the Commission's recommendations, and the Council adopted a resolution recommending action on Hoover Commission proposals.

The first Hoover Commission (1947-1949) recommended among other things the use of performance budgets, emphasizing work to be done rather than objects purchased; separation of current expenditures from capital outlays in budget estimates; the development of standards for performance budgets and management research functions; and the adoption of accrual accounting to the extent appropriate. The Commission

also recommended establishment of a new Accountant General in the Treasury Department to prescribe administrative accounts, subject to the approval of the Comptroller General.

Among recommendations of the second Hoover Commission (1953-1955) were continued use of performance budgeting, formulation and administration of agency budgets on a cost basis, annual appropriations based on accrued expenditures, and authorization for limited periods of continuing government programs not susceptible to the usual budget controls. Additional proposals dealt with improvement of accounting and auditing practices.

The Budget and Accounting Procedures Act of 1950 incorporated many of the basic recommendations of the first Hoover Commission. It provided for a modernized budget and accounting system, full disclosure of the results of federal financial operations, continuous study and improvement of the budget and accounting systems, and effective control over income and expenditures through an up-to-date audit program. This act was praised by the heads of federal fiscal agencies as the most progressive step forward in the improvement of the federal government's financial system since the Budget and Accounting Act of 1921.

However, the Congress rejected two major recommendations of the first Hoover Commission: one, that the budget show a separation of current and capital expenditures, and two, the creation of an Accountant General under the Secretary of the Treasury. This latter proposal was resisted by the Comptroller General on the ground that it would transfer to the executive branch a vital and substantial part of the function presently exercised by the General Accounting Office. The Secretary of the Treasury also opposed the suggested division of authority and indicated that the most fruitful results could be achieved through co-operation of the various agencies concerned. He referred to the existing co-operative relationship of the GAO, the Treasury, and the Budget Bureau and their agreement on general objectives.

The Budget and Accounting Procedure Act and other legis-

lation in 1949 gave the Comptroller General power to prescribe accounting requirements in terms of principles and standards, established controller functions in the Department of Defense, and relieved the GAO of the job of keeping the Post Office Department accounts, while providing for an independent audit of that Department by the GAO in accordance with prescribed principles and standards.

Many of the budget and accounting recommendations of the second Hoover Commission were incorporated in Public Law 863, 84th Congress, which was passed in 1956. This law provided for the use of cost-based budgeting and the maintenance of accounts on an accrual basis to show resources, liabilities, and costs of operations of each agency so as to facilitate preparation of cost-based budgets. Provision was also made to require adequate monetary property accounting records as an integral part of each agency's accounting system. The Congress, however, did not adopt the Commission's proposal to make annual appropriations on an accrued expenditure basis.

Many certified public accountants were members of Hoover Commission Task Forces. J. Harold Stewart, a past president of the Institute, headed the second commission's Budget and Accounting Task Force, and seven other CPAs were members or consultants of this group. Paul Grady, who had served as chairman of the Institute's committee on auditing procedure and had headed the Navy's cost-inspection service during World War II, was chairman of the Task Force on Lending Agencies. Other CPAs served as members of various Task Forces.

Thus, over a period of 13 years, beginning with the Conference on Federal Government Accounting in 1943, the accounting profession, through Institute committees and the efforts of individual members, had exercised a significant influence in improving the financial management and controls of the federal government. It should be noted, however, that many dedicated accountants within the government co-operated enthusiastically in the effort.

Thereafter, there was a lapse of Institute activity in this area.

Implementation of the new programs had to be accomplished internally—largely through the Joint Financial Management Improvement Program.

A New Comptroller General

In 1954 President Eisenhower nominated Joseph Campbell, a CPA and a member of the Institute, to be Comptroller General of the United States, succeeding Lindsay Warren, who retired. Mr. Campbell encouraged the trends begun under Mr. Warren toward modernization of accounting and auditing procedures, and toward building up a skilled staff of professional accountants, including at the conclusion of his term more than 2,000 college graduates, of whom about 400 were certified public accountants—some in top-level positions.

Mr. Campbell retired due to ill health in 1965. He was succeeded in March 1966 by Elmer B. Staats, then Deputy Director of the Bureau of the Budget, with whom the Institute continued close co-operative relationships, several of its members serving on an advisory council which Mr. Staats created to assist him.

The Joint Financial Management Improvement Program

In 1958, with the legislation incorporating many of the Hoover Commission recommendations as a base, the objectives of the Joint Program were defined more clearly than previously. They included establishment of effective agency accounting systems on an accrual basis to the fullest extent appropriate; establishment of cost-based budgeting practices effectively integrated with the accounts to provide adequate support for

budget requests; the use of consistent classifications to bring about effective co-ordination of agency programming, budgeting, accounting, and reporting practices; establishment of suitable internal control practices, including internal audit, in the agencies; effective integration of agency accounting and reporting with the requirements of the budget process and the central accounting and reporting of the Treasury Department; and development of accurate and useful agency and government-wide reports on fiscal status, financial results of operations, and cost of agency performance of assigned functions.

Reports of progress in the conduct of the Joint Program have been made annually. The twentieth annual report published in 1968 was an impressive summary of what had been accomplished. The scope of activity included accounting, cash management, central disbursing, reporting, internal and contract auditing, staffing and training.

The 1968 report said, "Prior to 1948 accounting in the federal government emphasized uniformity throughout the government and provided detailed fund controls. Preoccupation with fund controls and the legality of expenditures resulted in unnecessary paper work and duplicate record keeping, with little regard to managerial usefulness. Today the emphasis is on managerial accounting so that accounting might better fulfill its role as a service to management. Accrual accounting concepts have been widely adopted."

Integrated planning, programming, and budgeting systems in the executive agencies were initiated in 1965.

Management Audits

Partly as a result of the new legislation and partly as an outgrowth of the Joint Financial Management Improvement Program, the General Accounting Office undertook, in addition to its financial-control procedures, a program of management audits, or audits of management performance, designed to

evaluate the effectiveness of an agency's discharge of its responsibilities. These management audits involved an examination of organization, operation, and controls as well as financial results. Reports on management audits were submitted to Congress or to agency officials, generally depending on the significance of the findings.

The Commission on Budget Concepts

In 1968 President Johnson appointed a Commission on Budget Concepts, one of whose members was Robert M. Trueblood, a past president of the Institute. The Commission made 13 major recommendations, the most important being that a unified summary budget statement be used to replace the existing three or more competing concepts. The Commission's recommendations were adopted practically in totality. They were supported by endorsement of the Institute's executive committee.

The Federal Government Accountants Association

In the same year which saw enactment of the Budget and Accounting Procedures Act of 1950, a group of some 40 accountants employed in various agencies of the federal government formed the Federal Government Accountants Association. Its objectives were to aid in improvement of federal financial management, to conduct research which would lead to improved financial management techniques, and to attract higher quality personnel in the financial management areas. The membership grew rapidly, reaching more than 7,000 within the next 20 years, and chapters were formed in various cities throughout the country. More than 125 agencies or major divi-

sions thereof in the federal government were represented in the Association.

Many of the members were certified public accountants, and many of these were members of the American Institute of Certified Public Accountants. Co-operation between the Association and the Institute was a natural and productive result. Indeed, the FGAA maintained co-operative relations with all the leading national accounting organizations, since its interests ranged over auditing, financial reporting, cost accounting, and managerial accounting as applied to the problems of the federal government.

The existence of FGAA facilitated communication within the government agencies, and exchange of views on accounting and related problems. It also facilitated communication between the federal government accountants and those engaged in industry or professional public practice. Progress toward the objectives of the Joint Financial Management Improvement Program was expedited by the meetings and publications of the FGAA. Of the latter the most influential was the quarterly technical journal, *The Federal Accountant*. Technical meetings, seminars, and forum discussions both on a national and local scale afforded opportunities for useful exchange of ideas and information. A series of research studies in government-oriented financial management problems and concepts was initiated.

A major undertaking of FGAA was to encourage university-trained young people and other qualified accountants to enter the federal career service. Recruiting brochures, scholarship award programs, and meetings with faculty and students were directed to this objective.

Recognition of appropriate experience in accounting and auditing in the government service as meeting the experience requirements for the CPA certificate was a major goal of FGAA. The General Accounting Office and the Internal Revenue Service also made efforts in the same direction. As a result, an increasing number of states accepted appropriate types of government accounting experience as meeting the CPA requirement.

The Institute's Washington Office

Following acceptance by the GAO of commercial-type audits, the launching of the Joint Financial Management Improvement Program, and the adoption of many of the accounting recommendations of the two Hoover Commissions, the intensive efforts of the Institute to encourage improvement in federal government accounting came to an end for the time being. A great deal had been accomplished. Sound policies and programs had been adopted. It remained only to implement them. The implementation necessarily had to be accomplished internally, and since there were rapidly increasing numbers of CPAs in key positions in the various agencies, it was assumed quite properly that the job should be left to them.

From time to time, in the following years, Institute committees or task forces were asked to advise on specific problems involving financial controls, federal budgeting, cost determination for defense contract purposes, and specific problems of the regulatory agencies. Beyond general advice, however, committees of volunteers were not equipped to undertake studies or analyses of major proportions—unless it was done at great sacrifice to their firms and themselves. The Institute, on the other hand, had no staff facilities available for extensive research on governmental problems. Furthermore, continuity of personal acquaintance and communication was difficult in view of the frequent changes in personnel occupying key positions in the federal government, and equally frequent changes in the personnel of Institute committees.

From its New York headquarters it was difficult for the executive staff of the Institute to keep in touch with all the government officers who had accounting or auditing problems on which they might like assistance, and in the absence of personal relations many government officials in this position were not even aware of the availability of the Institute for advisory services.

It was clear that the federal government would have an increasing involvement with the private economy, and that in

this involvement many accounting, auditing, and reporting problems would arise. If the Institute was to have a voice in the decisions, it could not be accomplished through the sporadic and unco-ordinated efforts of numerous volunteer committees.

In 1959, therefore, the Institute established a Washington office, under the direction of Lyman Bryan, and a new committee on relations with the federal government to co-operate with the Washington staff and to co-ordinate the activities of special technical committees and individual consultants working on behalf of the Institute with individual agencies.

The charge to the Washington staff was not to lobby. It was instructed to serve as a liaison, an information center, and an early-warning system. Its director, Mr. Bryan, was to maintain personal relations with agency officials and Congressional committees concerned with any aspect of accounting; to make frequent reports to the executive office; and to assist the members of the committees dealing with technical problems in Washington. In addition the director prepared a monthly column in *The Journal of Accountancy,* reporting developments affecting the profession, and assisted individual members in finding answers to questions or in finding the right people to talk to in Washington.

The record of the Washington office over a ten-year period was impressive. It gave the Institute a visibility in the nation's capital which had not existed before. It provided the executive office and the committees with professional, experienced advice on the proper approaches to legislative or regulatory problems, and background on related political implications. It kept government officials and members of the Congress informed of developments in accounting of interest to them—which resulted in many expressions of appreciation—and kept the profession informed of emerging policies and actions in Congress or the agencies which might otherwise have been overlooked until it was too late.

One significant result was an increasing realization on the part of both Congress and many agencies that governmental

audit functions can often be carried out more effectively and economically by engagement of professional accounting firms than by recruiting and training internal audit staffs. A survey in 1958, for example, indicated only about ten federal agencies which were using outside accountants to any significant extent. Six years later it was discovered that 53 programs, conducted by 26 different federal agencies, resulted in about 38,000 annual engagements of outside accountants. By 1968 these numbers had increased to 30 agencies, 80 programs, and 51,000 annual engagements.

Furthermore, Washington officials learned that practicing certified public accountants could do other things than audit balance sheets and income statements, important and pervasive as this function was. For example, the Housing and Home Finance Agency arranged a program under which public accounting firms could certify costs of depressed-area projects. The Small Business Administration provided for extension of the financial audits of small-business investment companies conducted by CPAs to include a check on compliance with nonfinancial requirements in the law and regulations governing the SBICs.

Among other agencies requiring a significant number of independent financial audits annually—in addition to the SEC, which of course required the greatest number—were the Rural Electrification Administration (electric and telephone co-operatives), the Federal Home Loan Bank Board (federally insured savings and loan associations), and the Farm Credit Administration (reports to banks from farm co-operatives). Cost audits by independent auditors were also provided for under the Medicare program.

So frequently were provisions being inserted in laws or regulations requiring independent audits by outside accountants for one purpose or another that in 1960 the Institute proposed standard language for such requirements, in order to assure responsibility on the part of those conducting the audits. The Comptroller General and the Budget Bureau endorsed this

language, which has been used increasingly over the years. The model language follows:

> The accounts of (the entity) shall be audited (frequency) in accordance with generally accepted auditing standards by independent certified public accountants or licensed public accountants, certified or licensed by a regulatory authority of a state or other political subdivision of the United States.

Consulting services were provided through the Institute's technical committees and staff to many agencies, often at the suggestion or with the assistance of the Washington staff. Largely these consultations dealt with accounting requirements of the agencies, such as those embodied in uniform systems of accounts of the Interstate Commerce Commission and the Civil Aeronautics Board. Sometimes they involved accounting problems affecting the rate-making process, such as those with which the Federal Power Commission was concerned. There was frequent consultation with Defense Department officials on cost determinations for defense contract purposes. In 1968 the Institute authorized a major research project on cost accounting principles to be conducted by faculty of Stanford University under contract, partly in the hope of aiding the Defense Department in establishing cost guidelines, but also with many other applications in mind.

From time to time Institute committees reviewed the annual reports on the Joint Financial Management Improvement Program. Discussions were held with top officials of the three participating agencies, and those of other major agencies, such as the Department of Health, Education, and Welfare and the Defense Department, on possible additional improvements in government financial controls.

Local Government Accounting

In 1948 the National Committee on Municipal Accounting, which had been dormant during the war years, was reacti-

vated, the Institute's committee on municipal accounting was reconstituted, and the work of endeavoring to improve local government accounting, auditing, and financial reporting was resumed.

The increasing involvement of the Institute with accounting problems of the federal government and local governments over a quarter of a century is an excellent example of public service and public relations at the highest level. By associating itself with projects of significant import to the public, the CPA profession gained respect, understanding, and opportunities for increased service.

CHAPTER 17

Ethical Responsibilities

A CODE of ethics and the related official literature reflect responsibilities voluntarily assumed by a profession.

Enforcement of the code indicates the profession's good faith—the sincerity with which it declares its intention to protect the public interest.

In the early years accountants were reluctant to fence themselves in with rules or to subject themselves to discipline. There was much exhortation to behave in a manner worthy of professional men, but the exhortations were widely ignored. Advertising and solicitation were rife. Reports signed by accountants were justly criticized by bankers and other observers.

But, in the 1920's and early 1930's, there was a breakthrough; by 1936, the end of the profession's first 50 years in the United States, meaningful rules of conduct and enforcement procedures had come into being. Thereafter, extension of the existing rules and introduction of new ones were accelerated.

Twelve basic rules of professional conduct were effective in 1937. Briefly, they covered the following matters:

1. Use of the title "Members of the American Institute of Accountants."
2. Certification of statements containing essential misstatements, or omitting facts which would amount to essential misstatements, if either willful or as the result of such gross negligence as to be inexcusable.
3. Prohibiting another, not a member of the Institute or in association with a member, from practicing in the name of a member.
4. Giving or receiving commissions or brokerage, or participation in fees by "the laity."
5. Occupations incompatible with that of a public accountant.
6. Certification of statements not verified under the supervision of the member or one of his firm, or another member of the Institute, or a member of a foreign accounting organization of good standing.
7. Efforts to secure legislation without notifying the Institute.
8. Solicitation or encroachment on the practice of another member.
9. Offers of employment to employees of fellow members.
10. Contingent fees (not applicable to tax matters).
11. Advertising (only "cards" were permitted).
12. Participation in activities of schools whose promotional methods or other activities were discreditable to the profession.

These rules were supplemented by resolutions of the Council which, while expressing its view, did not have quite the same force as rules. In substance, these resolutions were as follows:

1. Audit companies and similar organizations were detrimental to the interests of the profession.
2. Public accountants should not permit their names to be used in conjunction with estimates of future earnings in a manner

which might suggest that the accountants vouched for the accuracy of the forecast.

3. No member should certify financial statements of any enterprise financed in whole or in part by the public distribution of securities if he were himself the actual or beneficial owner of a substantial financial interest in the enterprise or was committed to acquire such an interest.
4. Competitive bidding for professional engagements was contrary to the best interests of clients, the public, and the profession.

The enforcement procedures were, briefly, as follows: The committee on professional ethics, consisting of five members of the Council, elected annually by the Council, considered complaints against members. If it found a prima facie case showing violation of any bylaw or rule of conduct, or conduct discreditable to a public accountant, the matter was reported to the executive committee, which then summoned the member involved to appear in answer at the next meeting of the Council. The entire Council, then comprising about 40 members, sat as a Trial Board, and determined the guilt or innocence of the respondent. Punishment was admonition, suspension, or expulsion. A statement of the case and the decision of the Trial Board, either with or without the name of the person involved, was then prepared by the executive committee and published in *The Journal of Accountancy.*

These arrangements were not mere window-dressing. The Institute gave ample evidence that it was determined to enforce ethical standards. It disciplined many members, some of them from prominent firms. The membership as a whole supported the strong policy. The CPAs of the country, for the most part, had decided that they were going to make accounting a profession, not a business.

As the growth of the profession accelerated, and increasing demands on CPAs led to expansion of their services, extension and clarification of the rules became necessary, as well as redoubled efforts to assure compliance. Since voluntary compli-

ance with the rules was far more desirable than extensive policing activities, educational efforts were expanded, while effective disciplinary machinery was maintained.

Widening Scope of Activity

In 1939 the Securities and Exchange Commission consented to inform the Institute's committee of any action by the Commission involving questionable activities on the part of an Institute member, which then were investigated independently by the committee.

As a step in the program of education of members on ethical questions, the ethics committee's 1940 report to Council was supplemented by an analysis of cases and inquiries. Similar analyses were published in the *Year Book* annually until that publication was discontinued. Thereafter committee rulings were published in the monthly *CPA*.

The language of the bylaws left open the question whether the committee was required to await a formal complaint before it could investigate questionable conduct on the part of a member. In 1940 Council authorized the committee to investigate any matter coming to its attention through any channel which suggested the possibility of a violation of the rules.

As an additional incentive to voluntary compliance, the Council wisely decided in 1941 to involve the membership as a whole in the rule-making process. Prior to that time the Council had exercised its authority under the bylaws to promulgate rules of conduct unilaterally. In that year, however, it decided to submit proposed rules to the membership for a vote by mail ballot. Subsequently the bylaws were amended to require this procedure.

The workload of the ethics committee increased so rapidly that it sought authority to engage a paid assistant, first on a part-time basis. Later, a permanent member of the Institute staff was assigned to assist the ethics committee, in addition to other

duties. Still later, the ethics committee became a full-time staff assignment for one man, and then for several people. In 1968 the ethics committee received full divisional status in the Institute's organizational structure, with its own full-time staff of five persons.

By 1955 the volume of work was too much for a five-man committee. The bylaws were amended to remove any limitation on the size of the committee and to eliminate the requirement that its members be members of the Council. Immediately, the number of members was increased to 15, and gradually it grew to more than 40. The several phases of the work were divided among subcommittees.

As a safeguard against possible oversights—and possibly against getting too far ahead of the troops—the committee decided in 1957 to expose drafts of proposed new rules to members of the Institute's official family and to the state societies, in order that objections or misunderstandings might be revealed before the rules were submitted for formal action.

Also in 1957, the committee began the issuance of formal opinions interpreting the rules, the first five of which were issued in that year.

The activities of the ethics committee also imposed an unbearable workload on the Council sitting as a Trial Board. It was, therefore, decided to create a separate Trial Board, composed of 21 present or former members of the Council, empowered to act independently. By 1961 even this separate Trial Board had too much to do, and the bylaws were amended to permit small panels of the Trial Board to hear cases in different parts of the country and mete out penalties, subject to review on appeal by the entire Board.

Progress Toward Co-ordination

The lack of uniformity, and duplication of effort, in disciplinary proceedings among the state societies, the state boards,

and the Institute aroused concern. Several cases were noted in which members had been required to appear before all three bodies. In some of these cases the findings of the several tribunals were inconsistent with one another—partly because of differences of opinion, and partly as a result of differences in the language of the rules under which the cases were heard. A systematic effort was undertaken to achieve uniformity among the codes of ethics, to provide for exchanges of information between the state societies and the Institute, and to co-ordinate their actions. In 1963 a conference was arranged in conjunction with the annual meeting of the Institute, at which state society and Institute officials discussed ways and means of achieving effective compliance with minimal duplication of effort.

In 1966, Hilliard R. Giffen, incoming president of the Institute and head of the firm of Giffen, Hills & Carruth in Fresno, California, addressed the Association of CPA Examiners on the need for co-ordination in enforcement of the ethical rules. He reported the results of a survey conducted by the Institute indicating that some state societies and state boards were vigorously enforcing their rules, but in many states there was apparently only sporadic enforcement activity, or none at all.

A few months later President Giffen wrote to all the state societies and state boards of accountancy to emphasize his concern about the uneven extent of enforcement of ethical standards. He referred to an amendment of Treasury Department Circular 230, which left to the professional societies and licensing boards much of the supervision over the conduct of practitioners before the Department, which had formerly been the responsibility of its own Committee on Enrollment and Disbarment. This action on the part of the Treasury Department followed enactment of the law by Congress which automatically admitted lawyers and certified public accountants in good standing in their own states to practice before the Department (see Chapter 9). In his letter President Giffen stressed the desirability of a full exchange of information regarding disciplinary matters among the Institute, state boards, and state societies. The response was most encouraging. In its next re-

port to Council, the ethics committee expressed optimism about the prospect of uniformity in codes and elimination of duplication in disciplinary proceedings.

In the same year the first National Conference on Professional Ethics was held in October in New York. Representatives of state societies, state boards, and the Institute attended this two-day meeting. Addresses were made by officials of United States Government agencies, by Institute officers, and by state society representatives. The desirability of uniform codes and co-operation in enforcement were emphasized. A summary of the speeches and the resulting discussion was published and widely circulated. The prospects for co-ordinated effort and efficient division of labor seemed excellent as plans were made for a second National Conference on Ethics in the fall of 1969.

Ethics as an Examination Subject

The ethics committee noted with approval in 1964 that six state boards had required candidates to submit to a written examination in ethics in addition to the uniform CPA examination, that two others were considering similar requirements, and that a few other states were subjecting candidates to oral examinations on ethics. It was expected that other states would follow these examples.

Operating Problems

The ethics committee encountered some problems in pursuing its disciplinary objectives. It reported, for example, that members who were indicted for crimes involving moral turpitude could remain members in good standing until trials had been held and appeals had been heard by the courts—a process

which often consumed many years. In 1963 the committee proposed that members under indictment for such offenses be automatically suspended without prejudice until the final judicial determination of their cases had taken place. This proposal cleared the Council, but on submission to the membership was defeated.

The committee was often irritated by failure of recalcitrant members to respond to committee requests for information related to alleged misconduct. Under the existing bylaws the committee could not compel members to reply. An amendment to the bylaws was adopted to correct this situation, reading as follows:

> A member or associate renders himself liable to expulsion or suspension by the Trial Board or a sub-board thereof if . . . (g) he fails to co-operate with the committee on professional ethics in its efforts to ascertain the facts pertaining to whether such member or associate is subject to disciplinary action pursuant to the bylaws of the Institute. Accordingly, a member or associate shall respond to communications from the committee requesting information as to such facts within 30 days of the mailing of such communications by registered mail, postage prepaid, addressed to the member or associate concerned at his last known address, according to the records of the Institute.

It seemed to the ethics committee an unnecessary waste of time and money to hold Trial Board hearings when a member's CPA certificate had been suspended or revoked, or when he had been convicted of a felony. The committee proposed an amendment to the bylaws providing for automatic suspension or termination of membership in such cases. This proposal was revised by the executive committee to leave the Institute some discretion in cases involving suspension or revocation of CPA certificates if it appeared that the findings of the authorities outside the Institute had resulted in a miscarriage of justice. The result was a bylaw approved by the membership providing for automatic suspension in such cases with the exception that on the request of the member concerned the matter might be reviewed

by the Trial Board, which could waive the automatic suspension or termination of membership if it appeared that because of exceptional or unusual circumstances it would be inequitable to permit the automatic provision to be exercised.

Publications

As part of its educational activity in the field of ethics the Institute published three books: in 1946, *Professional Ethics of Public Accounting;* in 1956, *Professional Ethics of Certified Public Accountants;* and in 1966, *Ethical Standards of the Accounting Profession.* Thousands of copies lodged in the reference libraries of practitioners. At some colleges and universities, the books were used as supplementary texts in auditing courses. They were favorably reviewed in legal journals and other non-accounting publications and were the subject of favorable comment by bankers and government officials.

Overhauling the Rules

In addition to its day-to-day work, the ethics committee undertook several major overhauls of the rules of conduct. In 1940 a revision was approved incorporating resolutions of the Council as formal rules, which made a total of 15. In 1956 the rules were restudied with particular attention to ethical questions not yet covered and, for the first time, with consideration of applications to tax practice and management services.

This study resulted in a codification of the rules, including references to formal opinions of the ethics committee, in what was renamed the "Code of Professional Ethics."

This new Code began with a preamble, after which the rules were grouped under five main headings: Relations with Clients

and Public, Technical Standards, Promotional Practices, Operating Practices, and Relations with Fellow Members. Six years after the work had begun, the new Code was adopted by the membership.

In 1968 the committee undertook another formidable task—to restate ethical principles in affirmative terms. It was recognized that rules of the "thou shalt not" variety encouraged compliance only within the strict letter of the law—what might be considered a minimum standard of conduct. The committee sought a way of expressing officially the profession's aspirations to a higher level of behavior that it would not be possible to describe in formal rules. While the Institute committee was studying the possibilities, the American Bar Association published a proposed restatement of its own Canons of Ethics, which included statements of a relatively few general principles of ethics, supplemented by "ethical considerations" in abbreviated essay form, indicating the reasoning underlying the Canons and appropriate behavior in circumstances not covered by specific prohibitions. The formal Canons of Ethics were then restated—as minimum requirements—under the related general principles. The Institute's ethics committee decided to adopt a similar approach, and work was begun on this ambitious project in 1969.

Technical Standards

To a greater extent than in other professions, the ethical code of the accounting profession required conformity with an expanding body of technical standards. This was as it should be. Certified public accountants, in their capacity as independent auditors, are responsible not only to their own clients, but also to creditors, investors, and others who may rely upon the CPAs' reports. The public has a right to expect that failure to observe prevailing technical standards will be grounds for

discipline. Accordingly, the Institute found it necessary to extend, amend, and interpret its Code of Ethics as the body of technical standards expanded.

For example, the old Rule No. 2, adopted in May 1929, provided for discipline of a member who willfully, or through such gross negligence as to be inexcusable, certified financial statements which were misleading or omitted essential facts. But at that time there were no standards through which the ethics committee could determine what was considered misleading, or what was an omission of an essential fact. The committee complained, as noted in Volume I of this work, that cases had come before it in which it believed that Rule No. 2 had been violated, but that the presumed violations were not uncommon, and to single out one offender for discipline would be difficult. The committee deplored the lack of authoritative standards of financial reporting, failure to conform with which would be cause for discipline under Rule No. 2.

However, when the committees on accounting and auditing procedure began to issue bulletins, and the SEC continued to publish opinions and rulings, a body of authoritative auditing and financial-reporting standards was in fact evolving. Accordingly, in the 1940 revision of the Rules of Professional Conduct, the old Rule No. 2 was rewritten as Rule No. 5, in much more specific terms than formerly, as follows:

> In expressing an opinion on representations in financial statements which he has examined, a member or an associate shall be held guilty of an act discreditable to the profession if:
>
> (a) he fails to disclose a material fact known to him which is not disclosed in the financial statements but disclosure of which is necessary to make the financial statements not misleading; or
>
> (b) he fails to report any material misstatement known to him to appear in the financial statements; or
>
> (c) he is grossly negligent in the conduct of his examination or in making his report thereon; or
>
> (d) he fails to acquire sufficient information to warrant expression of an opinion, or his exceptions are sufficiently material to negative the expression of an opinion; or
>
> (e) he fails to direct attention to any material departure from gen-

erally accepted accounting principles or to disclose any material omission of generally accepted auditing procedure applicable in the circumstances.

This rule was far more readily enforceable than its predecessor. It marked progress in clarification of the independent auditor's responsibilities. Sub-paragraph (d), for example, reflected "Extensions of Auditing Procedure" (see Chapter 2). Sub-paragraph (e) took on added meaning in view of the mounting volume of technical pronouncements by the Institute and the SEC.

Statement on Auditing Procedure No. 23 (see Chapter 7), issued in 1947, required a member, when his name was associated with financial statements, either to express an opinion or to disclaim an opinion and explain why. Several years later a survey was conducted by the committee on auditing procedure to determine the extent of compliance. The survey was conducted with the co-operation of banks throughout the country, and involved examination of several thousand financial statements submitted for credit purposes. The findings indicated that about 20 per cent of auditors' opinions examined failed to comply with Statement No. 23.

This led to an addition to the rules of conduct requiring a member in public practice whose name was associated with financial statements to (1) express an unqualified opinion, or (2) express a qualified opinion, or (3) disclaim an opinion on the statements taken as a whole and indicate his reasons therefor. The rule also required that when unaudited financial statements were presented on his stationery without comment, the member disclose prominently on each page that the statements had not been audited.

This rule was later expanded, as a result of a later pronouncement of the committee on auditing procedure, to include a requirement that an "adverse opinion" should be expressed in cases where the auditor knew that the statements did not fairly present the situation, regardless of the fact that an incomplete audit or no audit might have been conducted. In turn these

requirements were supplemented by the committee on ethics in its Opinion No. 8, which stated that when a member believed financial statements were false and misleading, denial of an opinion was insufficient, and that the member should require adequate adjustments or disclosure of the facts, or refuse to permit his name to be associated with the statements in any way.

Thus by 1959 it was clear that a member could be disciplined for trying to evade responsibility through the use of ambiguous qualifying words or phrases, or by silence.

Another rule was challenged as inadequate in 1959—Rule No. 12 prohibiting association of a member's name with an estimate of future earnings contingent upon future transactions in a manner which suggested that he vouched for the accuracy of the forecast. After extensive debate, this rule was broadened in 1964 so as not to confine the prohibition to estimates of earnings. As amended, the rule prohibited association of a member's name with any forecast of the results of future transactions in a manner which might lead to the belief that he vouched for the accuracy of the forecast. The ethics committee interpreted this rule in Opinion No. 10, which made it clear that members were not prohibited from assisting clients in the preparation of budgets, financial forecasts, and other special-purpose financial data involving expression of expected results of future operations; however, on the presumption that such data might be submitted to parties other than the client (such as bankers), when a member's name was associated with such statements full disclosure must be made of the sources of information used, or the major assumptions made, in the preparation of the statements, the character of the work performed by the member, and the degree of responsibility he assumed, and it must be made clear that the member did not vouch for the accuracy of the forecast.

Another early rule of conduct had permitted reliance on the work of others than members or employees of a member's own firm, provided that such others were certified public accountants of the United States, or members of the Institute,

or of similar associations of good standing in a foreign country. This rule was designed to prevent members from signing reports based on audits conducted by unqualified accountants, which the members had not controlled, but at the same time to permit co-operation among members of the Institute and other CPAs, or among Institute members and reputable firms abroad, in the audit of organizations with far-flung branches or subsidiaries, some of which were situated in places where the Institute member concerned maintained no branch offices. In 1965, however, it was decided that this rule needed tightening. It was amended to provide that a member might utilize in part, to the extent appropriate in the circumstances, the reports or other evidence of auditing work performed by another CPA, or a firm of public accountants at least one of whom was a CPA, whose independence and professional reputation the member had ascertained to his satisfaction; and that a member might also utilize in part, to an appropriate extent, the work of public accountants in other countries, but in so doing must satisfy himself that such accountants were qualified and independent, that the work had been performed in accordance with generally accepted auditing standards prevailing in the United States, and that the financial statements were prepared in accordance with generally accepted accounting principles prevailing in the United States, or were accompanied by information necessary to bring such statements into accord with such principles. This revision put the burden of responsibility on the Institute member who relied on work performed by others. It closed the door to evasion of responsibility by casting blame on other accountants on whose work a member had relied without adequate investigation.

As narrated in Chapter 6, a special committee, acting under instructions of the Council, recommended that a rule of ethics be adopted requiring members to disclose departures from Opinions of the Accounting Principles Board. The recommendation was made in 1964, but action was delayed at the suggestion of the executive committee until the profession could adjust to the Council's resolution to the same effect. In 1968,

however, the executive committee recommended addition of the following rule, which was approved by Council in 1969 and submitted to the membership for vote by mail ballot:

> In expressing an opinion on representations in financial statements which he has examined, a member or associate may be held guilty of an act discreditable to the profession if: . . .
>
> (e) he fails to disclose in his report, when material in effect: . . .
>
> (2) the use of any accounting principle which departs from generally accepted accounting principles because it lacks substantial authoritative support, in which case he must also either qualify his opinion or give an adverse opinion as appropriate; or
>
> (3) unless otherwise disclosed in the financial statements, the use of any generally accepted accounting principle which differs from an Opinion of the Accounting Principles Board but which has other substantial authoritative support.
>
> Disclosure must be made in his report or in the financial statements of the approximate effect of departures under (2) and (3), or a statement made as to the impracticability of determining such effect.

To the astonishment of the executive committee, the proposed rule failed to gain the approval of the required two-thirds of the members voting—it missed by about one-half of one per cent. Only slightly more than half of all the members voted—a familiar response in democratic organizations. Of those who did vote, 33.9 per cent were negative—just enough to prevent adoption of the rule.

No significant opposition had been expressed at the Council meeting or at the annual meeting in the fall of 1969, where the proposed rule was presented for discussion. Perhaps those who voted "no" simply did not want to be bothered by a requirement to understand and apply the sometimes complicated APB Opinions—many of which might appear not applicable to the practice of some CPAs.

Actually, the failure of the new rule to pass did not change things much. Article 2.02 of the Code of Ethics already required disclosure of any material departure from generally accepted accounting principles. The Council's action declaring

that APB Opinions constituted generally accepted accounting principles, and calling for disclosure of departure from such Opinions, would put any member who failed to comply in an extremely awkward position. If such failure came before the courts the position could be more than awkward.

However, the failure of the new rule to pass did leave the situation in some confusion, and it could be expected that the proposal would be resubmitted for another vote. Recalling initial membership resistance to the requirement in Statement on Auditing Procedure No. 23 and to the rule on independence, both of which were later approved by overwhelming majorities, it could be predicted that, after more discussion and explanation, a rule requiring disclosure of departures from APB Opinions would ultimately be adopted.

Such a rule would put the capstone on the series of reporting requirements initiated in 1939, which subjected members to discipline for failure to state clearly the responsibility they assumed for the fairness of financial statements with which their names were associated.

Practice Review

Reference has already been made in Chapter 7 to the practice review committee, which communicated with members who had expressed opinions on financial statements which appeared not to conform with prevailing technical standards. The committee pointed out the presumed faults and invited explanations. The objective was education, not discipline. This work was conducted in complete confidence and with assurance that the practice review committee would not refer any items it received to the committee on professional ethics. The ethics committee was in complete accord with this procedure, and in a report to Council stated that it would refer to the practice review committee any complaint involving technical questions

which did not constitute a clear violation of the Code, but with regard to which some question of substandard performance might exist.

Independence

The evolving concept of independence, and the debates and discussions bearing on independence, have been discussed at length in Chapter 8. The ethics committee was, of course, inevitably involved in all the steps taken to clarify the Institute's position on independence.

The committee's concern with this subject, however, predates even the SEC's first rule on independence. A recommendation in 1932 was rejected by the Council. In 1934, however, after the SEC had acted, Council was persuaded to adopt a resolution prohibiting a member from having a financial interest in a publicly financed enterprise of which he was independent auditor. This was incorporated in the Rules of Professional Conduct as revised in 1940.

In 1948 the committee reported that it was studying the possibility of an amendment to this rule, either forbidding a member to serve as an auditor of an enterprise conducted for profit if he were also a director of such enterprise, or, possibly requiring disclosure of the fact that he served as a director. Apparently the committee received little encouragement, despite the fact that an SEC rule prohibiting such joint service had been on the books for 15 years.

In 1952 a question was raised again as to the adequacy of the existing rule on independence, since it was limited to the question of financial interest and contained no guidance on the general concept of independence. However, the committee apparently concluded that the environment was not hospitable to change at that time.

In 1959, as recited in Chapter 8, the committee on ethics

vigorously advocated a new and comprehensive rule on independence, prohibiting any financial interest in any audit client—public or closely held—and joint service as auditor and officer or director of such a company. At the 1960 annual meeting, action on this rule was deferred, but at the 1961 meeting it was passed by a resounding majority and then was approved by more than two-thirds of the members voting by mail ballot.

Immediately thereafter, the ethics committee issued its ground-breaking Opinion No. 12, which in effect introduced a new measure by which the *appearance* of lack of independence could be judged.

The new rule stated that it was the auditor's responsibility to avoid relationships which "to one who had knowledge of all the facts" might appear to impair independence. Opinion No. 12 defined such relationships as those which to a "reasonable observer" who had knowledge of all the facts might suggest "conflict of interest" which might impair the auditor's objectivity.

Independence *in fact* was an attitude of mind, the committee said, but it recognized as of the utmost importance that the public have confidence in the objectivity of CPAs in expressing opinions on financial statements. To maintain such confidence, it was imperative to avoid relationships which might have the appearance of a conflict of interest: it was this reasoning, said the committee, which led to the prohibitions against having a financial interest in and acting as an officer or director of audit clients. However, the committee said in Opinion No. 12, it was not suggesting that the rendering of professional services other than the independent audit would suggest to a reasonable observer a conflict of interest. In management services and tax practice, so long as the CPAs' services were limited to advice and technical assistance, and a decision-making role were avoided, the committee saw no likelihood of a conflict of interest arising.

In 1964 the committee considered the appropriate type of report to be rendered by a member who was not considered independent by reason of possession of a financial interest in or

service as an officer or director of the client company, but nevertheless had prepared or examined the financial statements. After consultation with the committee on auditing procedure, the ethics committee published its Opinion No. 15, to the effect that such a member should state in his report that his examination was not conducted in accordance with generally accepted auditing standards (which required independence), and that he was therefore precluded from expressing an opinion on the financial statements.

In 1965 the committee considered elimination of the exception in the independence rule related to service as a director of a non-profit organization. Eleven members favored elimination—five were opposed. In view of this difference of opinion within the committee, the matter was referred to the executive committee, which recommended against elimination of the exception, at least for the time being. The executive committee pointed out that the exception was applicable only when it was clear that the duties performed as a director of a charitable, religious, civic, or similar organization were such as to make it clear that the member could express an independent opinion on the financial statements. To the majority it did not seem necessary to require members who audited such institutions to resign from the boards if membership thereon was largely honorary or simply signified sponsorship of the organization.

Another question relating to independence arose in the early days of Medicare. The Department of Health, Education and Welfare asked the Institute's committee on ethics whether an independent certified public accountant who served as auditor for a "provider"—such as a hospital—could also act on behalf of the "intermediary"—Blue Cross or an insurance company which represented the government in administration of the program—in auditing reimbursable costs of the same provider. The committee referred to a resolution of the Council, adopted in 1944, to the effect that a CPA might properly undertake accounting or auditing engagements on behalf of government agencies or others involving the accounts of a regular client,

provided his relationship to the various parties was fully disclosed. This conclusion was based on the assumption that the certified public accountant would be as independent in the one capacity as in the other. Accordingly, the committee in 1966 advised the Department of Health, Education and Welfare that it was proper for a CPA to audit reimbursable costs of a hospital, for example, on behalf of the intermediary concerned, even though he or his firm were auditors of the hospital.

This response was not satisfactory to some members of the ethics committee or to some other members of the Institute who thought that such relationships would be inconsistent with the more recent Opinion No. 12, urging avoidance of relationships that to a reasonable observer in possession of all the facts might suggest a conflict of interest. On the other hand, it was argued that the intermediary must have complete confidence in the accounting firm which it engaged to review reimbursable costs of providers: the intermediary should have no reason to doubt the independence of that firm in reporting on the costs of a hospital on whose financial statements the firm had expressed an opinion.

This situation seemed to differ from one in which credit grantors generally, or investors generally, might rely on financial statements audited by an accounting firm with which they had no direct relationship. In the Medicare environment, the intermediary was in control: if it saw no conflict of interest, no one else was necessarily involved; if it did suspect such a conflict, it could require a review of the hospital costs by others than the accounting firm concerned.

This response, however, also failed to satisfy all the dissidents. At the time of this writing, the debate continues in some quarters.

The question arose whether a firm's independence would be impaired if a retired partner became a director or a stockholder of an audit client of that firm. In Opinion No. 16 the committee ruled that if a retired partner remained active in the affairs of the firm, even though not officially, the independence of the firm would be impaired if he were an officer,

director, stockholder, or key employee of a client on whose financial statements the firm expressed an opinion; however, if a retired partner were no longer active in the firm, regardless of the fact that he received retirement benefits, the independence of the firm would not be impaired, provided that the fees received from such a client did not have a material effect on the retired partner's retirement benefits and that he was not held out as being associated with the firm.

Promotion, Publicity and Encroachment

The Institute's first formal rule against advertising, adopted in 1922, permitted the publication in newspapers and other media of what were known as "cards"—simple boxes, limited in size, stating merely the name, the professional credentials, the class of service, and the address of the advertiser, or, in the case of change of address or personnel of a firm, a plain statement of the fact for publication of which the announcement purported to be made.

Twenty-two years later the committee on ethics proposed that the publication of cards as a regular practice be prohibited, and that they be permitted only for announcement of change of address or personnel of firm. An amendment to this effect was approved and became effective in 1945. Thirteen years after this step, the publication of such cards for any purpose was prohibited. The membership was convinced that there was no need for public advertisement of changes of address or personnel, since clients and personal friends could be informed of such changes directly.

In the early 1940's, the rules were amended to prohibit listings in directories by members of the Institute in bold type or in any other manner which differentiated them from other names in the same lists.

Some publishers had succeeded in selling to some members of the Institute what were known as "canned newsletters," to

be sent to clients and personal acquaintances. Most of these newsletters were concerned with tax matters. The name of a member's firm could be printed on the cover, conveying the impression that the firm was the author of the material. In 1953 the committee on ethics expressed its disapproval of the use of such "boiler plate," and published its views in *The Certified Public Accountant.* These views were repeated in the committee's first formal numbered opinion, entitled "Impropriety of Member's Furnishing Clients and Others with Tax and Similar Booklets Prepared by Others and Imprinted with Firm Name of Member."

The committee also considered the appropriate scope of distribution of material actually prepared by a firm itself—such as so-called "house organs," or publications on taxes, accounting, or subjects of general business interest. Distribution of such material, said the committee in Opinion No. 9, should be restricted to clients and individuals with whom professional contacts were maintained, such as lawyers of clients, and bankers; though copies might also be supplied to non-clients who specifically requested them, and to universities if the material was of educational value—always provided that the material did not advertise the professional attainments or services of the firm which produced it.

The question arose whether a member who wrote a book or article might permit the publisher to describe his professional qualifications and his firm affiliation. In its Opinion No. 4, the ethics committee held that the publication of such information was not a violation of the rule against advertising, but that the member was responsible for ascertaining that the publisher kept within the bounds of professional dignity and did not make claims that were not factual or not in good taste.

In 1962 the committee issued its Opinion No. 11, a comprehensive summary of previous rulings relating to advertising, announcements, directories, business stationery, business cards, and office premises. Later the opinion was amended to include a prohibition against including the name of a member's firm in a help-wanted advertisement, although the inclusion of tele-

phone number, address, or a box number was held to be permissible.

The original rule on solicitation stated simply that a member should not directly or indirectly solicit the clients or encroach upon the practice of another public accountant, but that it was the right of any member or associate to give proper service and advice to those asking such service or advice. Later this rule was modified by an amendment to read as follows:

> A member or associate shall not directly or indirectly solicit clients by circulars or advertisements, nor by personal communication or interview *not warranted by existing personal relations,* and he shall not encroach upon the practice of another public accountant. A member or associate may furnish advice to those who request it. [Emphasis supplied]

Later the ethics committee objected to the phrase "not warranted by personal relations," as a rather wide loophole. It also suggested that solicitation was of itself unprofessional, whether or not the object was the client of another public accountant. As a consequence, the rule was finally amended to read simply:

> A member or an associate shall not endeavor, directly or indirectly, to obtain clients by solicitation.

This rule was buttressed by five formal opinions, several of which have already been mentioned in the discussion of advertising. Opinion No. 2, however, made it clear that a member could not cause others to carry out on his behalf acts which, if carried out by the member, would place him in violation of the Institute's Code. For example, a member could not permit a trade association to advertise his services to its members.

The zealous efforts of the ethics committee to tighten up the rules were not always supported by the membership. In 1958 the committee proposed that a member who was approached by the client of another member, with a view to replacing the latter, should not accept the engagement with-

out giving prior notice to the predecessor accountant. It was understood that this was the general practice in England. This proposal was rejected by the membership.

As the scope of accounting practice widened, specialization increased rapidly. It seemed desirable for smaller firms, which could not maintain specialists in all areas, to refer their clients to other firms, or to call in specialists from other firms, when problems arose with which the small firms were not competent to deal. To overcome natural reluctance to refer a client to another firm which might take over all accounting services required by the client, a new rule was adopted. It provided that a member who received an engagement for services by referral from another member should not discuss or accept an extension of his services beyond the specific engagement without first consulting with the referring member. However, a proposal to strengthen this rule further, by forbidding the member who received an engagement by referral from accepting any extension of such services without the consent of the referring member, was rejected.

As the profession became the object of increasing attention by the public press, newspaper reporters, magazine writers, and editors sought interviews with members who for one reason or another seemed newsworthy at the time. The resulting news items or articles often contained descriptions of the members' firms and their activities. Other members of the Institute objected to such publicity on the ground that it amounted to advertising. At length the ethics committee amended its Opinion No. 9 to the following general effect: Statements by CPAs which were on subjects of public interest and contributed to public awareness of the profession were to be encouraged. However, members who became aware that their names or the names of their firms were to be mentioned in the public press or in magazine articles should apprise the author of the limitations imposed by the Code of Ethics, and "efforts should be made to assist the author to the end" that the articles did not "glorify" the individual firm or "distinguish it from others in practice." Information regarding the size of the firm, types of

services which it rendered, clients that were being served, location of offices, and so forth, the opinion said, served no purpose other than to glorify the firm; deliberate cultivation of publicity with respect to professional attainments constituted a clear violation of the rule against advertising.

This opinion, in turn, was the object of criticism by journalists and editors, as well as by some members. They argued that the limitations put members in the position of refusing to impart information of public interest, which the interviewer, in most cases, could obtain from other sources anyway, though with greater difficulty. The profession's desire for better public relations seemed thwarted in part by a rule which journalists considered an obstacle to the dissemination of legitimate information. With these considerations in mind, the executive committee requested, in 1966, that the ethics committee review this portion of Opinion No. 9. The committee at first balked. Its report to the Council said:

> At the suggestion of the executive committee, the ethics committee reviewed its Opinion No. 9. . . . The thought has been expressed that the final section . . . tends to block the release to the public of important information about the profession—information which the public has every right to know, and that . . . it effectively silences the member by forbidding him to give the very kind of information which the author wants. . . .
>
> After careful examination of Opinion No. 9, it was the committee's view that there is no need to revise the opinion at this time. . . .
>
> The committee still feels that while a member may co-operate with an author, information regarding size of the firm, types of services which it renders, clients being served, location of offices, etc., serves no purpose other than to glorify the firm in the eyes of the reader, and constitutes advertising. . . .

In the following year, however, representatives of the executive committee and the ethics committee met to discuss the problem. As a result the relevant section of Opinion No. 9 was revised to read as follows:

> Statements made by CPAs on subjects of public interest which are reported in the press and thereby contribute to public awareness of

the profession are not considered advertising and are encouraged.
Publicity deliberately cultivated either directly or indirectly by a member which advertises his or his firm's professional attainments or services is considered to be in violation of Rule 3.01 [advertising].

This change removed the limitation on what a member might say in answering the questions of a journalist, but it emphasized that initiation of publicity by a member, as contrasted with responses to unsolicited approaches by journalists, would be considered advertising.

Competitive Bidding

Competitive bidding for professional engagements, especially audit engagements, was considered a serious evil from the earliest days of the profession. Speeches and articles reiterated the damaging effects of price competition in a profession: it tended to downgrade the quality of services, it tempted practitioners to cut corners in an effort to keep their costs within the quoted price, and it tended to drive audit engagements into the hands of the least competent or the least scrupulous practitioners.

In 1934 the Council adopted a resolution to the effect that competitive bidding was contrary to the best interests of members' clients and of the public generally. Members were urged by all the means at their disposal to discourage the practice.

Some of the state societies adopted more stringent rules against competitive bidding. In 1938 the Connecticut Society of Certified Public Accountants complained that members of the Institute from other states had entered Connecticut and had ignored its rule prohibiting competitive bidding. In response the Council adopted the following resolution:

Resolved, That competitive bidding by a member or associate on work to be done in any state, territory or the District of Columbia,

> where the governing body of certified public accountants has adopted a rule prohibiting competitive bidding, may be considered an act discreditable to the profession.

The substance of this resolution was subsequently incorporated in a formal rule.

In 1951 the ethics committee expressed the belief that competitive bids should be prohibited under *any* circumstances, rather than only where bidding would violate a local rule. After consultation with legal counsel—and despite some qualms on his part—the committee proposed the following new rule, which was adopted by the members with enthusiasm:

> A member shall not make a competitive bid for a professional engagement. Competitive bidding for public accounting services is not in the public interest, is a form of solicitation, and is unprofessional.

The need for interpretation was apparent, and the ethics committee committed itself to publishing an opinion on the subject in the near future. The task proved more difficult than had been expected, however. The distinction between a competitive bid and an "estimate in good faith," in all the possible circumstances which might arise in practice, was not an easy one to draw. In addition, legal counsel warned of the danger of unintentional violation of the anti-trust laws.

Just as a draft interpretation satisfactory to the committee was exposed to state societies and others for comment, the California Society of Certified Public Accountants urgently requested that publication be deferred. The society's rule on competitive bidding had been challenged by the state attorney-general as a violation of the state anti-trust law. In the light of this report, the advice of the executive committee was sought. Conferences were held with legal counsel for the Institute and with another outstanding law firm, which had been called in for special consultation.

Counsel stated that recent trends in the Department of

Justice, and recent decisions of the courts, made it likely that enforcement of the rule against bidding would evoke charges of violation of the anti-trust laws. The lawyers strongly urged repeal of the rule. The Institute's officers, the executive committee, and the ethics committee were reluctant to accept this advice. The lawyers were challenged at every point. Ultimately, however, the two committees were completely convinced that the danger was serious. They recommended to the Council that the rule be repealed.

A stormy session of Council followed. Strong opposition to repeal of the rule was voiced. Legal counsel appeared and reiterated their arguments. Finally, in May 1966, the Council recommended repeal by a vote of 135 to 53.

The matter was then presented for discussion at the annual meeting in Boston in 1966. The debate was lively and protracted; a wide division of opinion was evident.

In accordance with the bylaws, however, the proposal to repeal the rule was submitted to all the members for vote by mail ballot.

Only a few more than the required one-third of the members returned mail ballots. Of these, 52 per cent favored repeal, but the required two-thirds vote to amend the Code was not obtained. The rule therefore remained on the books. Legal counsel then advised a public announcement that the rule would not be enforced.

While this advice was being considered the Institute was notified that the Justice Department was undertaking a preliminary investigation of complaints on the competitive bidding rule. Legal counsel conferred with the Justice Department, and again urged the Institute to announce that the rule would not be enforced.

At the following Council meeting in May 1967 the executive committee recommended such an announcement. The ethics committee concurred in the recommendation. Another debate ensued, revealing violent dissent by a minority. The majority approved the announcement, however, and it was pub-

lished as a footnote to the rule on bidding in the Code of Ethics, as follows:

> On the advice of legal counsel that Rule 3.03 subjects the Institute and its representatives to risks under the federal antitrust laws, the Institute's executive committee, Council and committee on professional ethics have decided that the Institute will continue to refrain from taking any disciplinary action against any member or associate under Rule 3.03 until there has been a change in circumstances that would justify a different opinion on the legal status of the Rule.

Up to the time of this writing, no further communication had been received from the Department of Justice.

Meanwhile, the ethics committee, with the approval of legal counsel, had published its Opinion No. 18, stating that quotation of a fee in advance of an engagement in an amount clearly inadequate to provide fair compensation for performing the service in accordance with accepted professional standards might be regarded in some circumstances as evidence of solicitation—and thus as a violation of the rule against that practice.

Practice in Corporate Form

In the old days corporations engaged in the practice of accounting were not uncommon. Generally referred to as "audit companies," some of them included stockholders who were not accountants. It was recognized that situations of this kind were inconsistent with claims to professional status.

Leaders of the Institute launched a campaign to eliminate practice by audit companies. There was resistance, however, and the first efforts were unsuccessful. During the discussion it was said that there was no objection to incorporation of accounting practices so long as all the officers and stockholders were certified public accountants, but the participation of laymen in what should be a professional practice was intolerable.

Finally, the Council resolved that audit companies and simi-

lar organizations were detrimental to the best interests of the accounting profession.

In 1938 the ethics committee said in its report to the Council:

> Twenty years ago the American Institute of Accountants expressed disapproval of the practice of accounting by auditing companies and similar organizations. Since that time a number of states have adopted legislation prohibiting the practice of accounting by corporations, and other states have forbidden the use of the CPA designation by corporations.

The committee suggested that the time had come when a definite rule should be adopted prohibiting members from affiliation with corporations engaged in accounting. The Council approved, such a rule was adopted, and for nearly two decades it remained unchallenged.

With the advent of data-processing equipment some members of the Institute desired to form separate organizations, as "service bureaus," in order to make this type of equipment available to their communities in competition with commercial organizations.

In its Opinion No. 7, issued in 1958, the committee on professional ethics stated that the type of service rendered through the use of data-processing equipment was similar to so-called "write-up work" or bookkeeping service as rendered by many public accountants. Therefore the committee held that any separate organization in which a member had an interest should not be permitted to do things which the member in public practice was prohibited from doing, such as advertising, soliciting business, or *practicing in corporate form.* This decision was supported by an existing rule of conduct to the effect that a member engaged in an occupation in which he rendered services of a type performed by public accountants, or rendered other professional services, must observe the bylaws and rules of professional conduct of the Institute in the conduct of that occupation.

Before long, however, computers came into general usage. Some members saw opportunities for the accounting profes-

sion in combining the skills of the certified public accountant with the greatly expanded capacity of computers for data processing. However, the cost of the equipment was so great that most local accounting firms could not afford to lease or purchase computers if the rules limited their use to existing clients.

It was proposed, therefore, that members or groups of members be permitted to purchase or lease computers and offer the use of the equipment only to their own clients and to other CPAs. This could be accomplished most conveniently by forming corporations to own the equipment.

In 1966 the ethics committee reported as follows:

> Typical of these inquiries is that involving two Institute members who formed a corporation to purchase EDP equipment and to perform computerized accounting services for other practicing CPAs. The corporation did not deal directly with the public, but it circularized other CPAs offering them the services in question. It was argued that since the members were not offering services to the public, they were not in the practice of public accounting and that consequently the prohibitions against solicitation and corporate practice did not apply.

However, the committee concluded that the members in question were in fact practicing public accounting, and so could not use the corporate structure, and that since the practicing CPAs for whom the EDP services were to be performed would be "clients" they could not properly be solicited.

Because of the importance of these decisions, the committee deferred implementation until the executive committee had been consulted.

The executive committee appointed a subcommittee to consider the matter, and after hearing its report reached conclusions contrary to those of the ethics committee. After a year of discussion, during which officers of the Institute met with the ethics committee, Opinion No. 7 was modified to this effect:

1. Practitioners could not perform data-processing services in corporate form for the public.

2. Data-processing services offered solely to practitioners could be offered by members in corporate form, but, since advertising would come to the attention of the public, such a corporation could call attention to its services only by direct communication with other practitioners.
3. The offering of "block time" on data-processing equipment did not constitute the practice of public accounting, so long as it did not entail systems design, programming, or service of any kind, but solely the use of the equipment; accordingly, the availability of "block time" could be advertised, provided the names of CPAs and the fact that CPAs were involved were not disclosed, but the offering of "block time" must not be used as a feeder to the member's practice.

This conclusion seemed a reasonable solution of a complex problem.

Meanwhile, pressures had come from other directions to encourage the practice of accounting in corporate form. Partnerships suffered many tax disadvantages in contrast with corporations—notably the inability to provide pensions for the partners through contributions currently deductible for tax purposes. A number of states had passed laws permitting the practice of professions in the form of corporations or in what were known as "professional service associations," which possessed many of the characteristics of corporations. It was believed that the courts would uphold the right of such professional associations, organized under state law, to be taxed as corporations. Typically the laws provided that only members of the profession concerned could be stockholders or officers of the corporation or professional service association, and that they would not be immune from personal legal liability for professional malfeasance.

In 1961 the ethics committee expressed the opinion that participation by a member of the Institute in such a corporation or professional association would be a violation of the Institute's rule against incorporation. Shortly afterward, however, the question was referred to the executive committee for considera-

tion on broad policy grounds. To study this matter the executive committee appointed an ad hoc group consisting of representatives of the ethics committee, the tax committee, and the executive committee itself. The views of public-relations counsel were also solicited. The ad hoc group concluded that for the time being, at least, it did not seem advisable to modify the Institute's rule by permitting members to incorporate under the professional association laws. The published report on this matter, however, made it clear that in the light of future developments this decision might be modified.

For one thing, it was not certain at that time whether the expected tax advantages of the new form of professional organization would be realized. But one of the most compelling arguments against changing the rule was the effect that incorporation might have on the public's attitude toward accounting as a profession. In view of the wide third-party interest in independent audits, it was felt that certified public accountants might be even more vulnerable to unfavorable public reaction than physicians or lawyers if it were assumed that financial considerations dominated the approach to practice.

The conclusion of the ad hoc group was unpopular among many Institute members who were eager to achieve the tax status enjoyed by corporations, but the decision was accepted for several years without strong opposition.

During these years, however, several lawsuits against accounting firms had thoroughly alarmed the profession. The size of claims being made, the decisions of some courts on preliminary motions, the attitudes of juries, and in some cases what seemed a punitive approach on the part of the SEC indicated that the financial liability of a certified public accountant was unlimited—that the personal fortunes of all partners of a firm might be wiped out by a verdict arising from a single instance of human error.

Marvin Stone, who became president of the Institute in 1967, had urged modification of the Institute's rule against incorporation in order that members could protect themselves against unlimited personal liability. He was less interested in

the possible tax advantages of incorporation than in the liability threat.

Largely as a result of his persuasion, the executive committee re-examined every phase of the question. A debate on the subject was held at the spring Council meeting in 1967. Thereafter an article was published in *The Journal of Accountancy* summarizing all known arguments for and against practice in the corporate form. Reprints of the article were sent to a cross-section of the profession, and to influential observers outside.

As a result of all the reactions, the executive committee recommended that the rule against incorporation be modified so as to permit practice in the corporate form, subject to certain safeguards which the ethics committee had developed. At a meeting in 1969, the Council approved amendment of the existing rule against incorporation to read as follows:

> A member or associate may offer services of a type performed by public accountants only in the form of either a proprietorship, or a partnership, or a professional corporation or association whose characteristics conform to resolutions of Council.

In conjunction with this action Council adopted the following resolution:

> WHEREAS, If the membership of the Institute approves the proposed amendment of Rule 4.06 of the Code of Professional Ethics permitting the practice of public accounting in the form of a professional corporation or association whose characteristics shall be established by the Council, it is hereby
>
> *Resolved,* That members may be officers, directors, stockholders, representatives or agents of a corporation offering services of a type performed by public accountants only when the professional corporation or association has the following characteristics:
>
> (1) *Name.* The name under which the professional corporation or association renders professional services shall contain only the names of one or more of the present or former shareholders or of partners who were associated with a predecessor accounting firm. Impersonal or fictitious names, as well as names which indicate a speciality, are prohibited.
>
> (2) *Purpose.* The professional corporation or association shall not

provide services that are incompatible with the practice of public accounting.

(3) *Ownership.* All shareholders of the corporation or association shall be persons duly qualified to practice as a certified public accountant in a state or territory of the United States or the District of Columbia. Shareholders shall at all times own their shares in their own right, and shall be the beneficial owners of the equity capital ascribed to them.

(4) *Transfer of Shares.* Provision shall be made requiring any shareholder who ceases to be eligible to be a shareholder to dispose of all his shares within a reasonable period to a person qualified to be a shareholder or to the corporation or association.

(5) *Directors and Officers.* The principal executive officer shall be a shareholder and a director, and to the extent possible, all other directors and officers shall be certified public accountants. Lay directors and officers shall not exercise any authority whatsoever over professional matters.

(6) *Conduct.* The right to practice as a corporation or association shall not change the obligation of its shareholders, directors, officers and other employees to comply with the standards of professional conduct established by the American Institute of Certified Public Accountants.

(7) *Liability.* The stockholders of professional corporations or associations shall be jointly and severally liable for the acts of a corporation or association, or its employees—except where professional liability insurance is carried, or capitalization is maintained, in amounts deemed sufficient to offer adequate protection to the public. Liability shall not be limited by the formation of subsidiary or affiliated corporations or associations each with its own limited and unrelated liability.

Subsequently the executive committee issued the following interpretation of the clause "amounts deemed sufficient to offer adequate protection to the public":

> *Resolved,* That professional liability insurance or capitalization in the amount of $50,000 per shareholder/officer and professional employee to a maximum of $2,000,000 would offer adequate protection to the public.

On balance, the acceptability of the $50,000 multiple to legislatures which had considered limitations on the liability

of professionals, and the absence of successful claims against accountants in excess of $2 million led the executive committee to the conclusion that this formula would attract public support, and therefore would be the most reasonable position to take in lieu of an amount or formula logically related to the risk involved in any one engagement.

Confidential Relationship

Until 1941 there was no rule prohibiting violation of the confidential relationship with clients—it was taken for granted that all CPAs would observe this basic requirement of professional practice. However, in that year it came to attention that a member had disclosed to a third party information about a client's affairs which had been acquired in the course of the member's professional work. This incident highlighted the absence of any rule on the subject. The ethics committee said in a report to Council:

> The necessity for preservation of this relationship seems so obvious to your committee as hardly to require elaboration, but since the rules of conduct purport to indicate cardinal points which members of the Institute should bear in mind, the committee concluded that it might be desirable to add to the rules a statement on this subject.

The following rule was proposed:

> All information concerning his client's affairs which a member has acquired shall be considered confidential. Except as disclosure may be required by legal process, no member shall directly or indirectly furnish a third party with any information with respect thereto without the consent of his client.

The Council approved the proposal in principle, but preferred a rule couched in more general terms.

The following rule was finally adopted after considerable discussion:

> A member or an associate shall not violate the confidential relationship between himself and his client.

Questions arose in later years which indicated a need for interpretation of this broad admonition. In Statement on Auditing Procedure No. 41, "Subsequent Discovery of Facts Existing at the Date of the Auditor's Report," the committee on auditing procedure described one kind of situation regarded as an exception to the general rule. The committee on professional ethics was also studying the matter as this book was written, in conjunction with the pending revision of the Code of Ethics.

Contingent Fees

The question was raised in 1941 whether the rule on contingent fees applied to situations such as bankruptcy cases, in which the fees of attorneys, accountants and other professional assistants were fixed by the courts. At the recommendation of the ethics committee, the rule was amended by adding to the exception covering tax cases the following sentence:

> Fees to be fixed by courts or other public authorities, which are therefore of an indeterminate amount at the time when an engagement is undertaken, are not regarded as contingent fees within the meaning of this rule.

Related Occupations

A new rule was adopted in 1948, providing that a member engaged in an occupation in which he rendered services of a type commonly rendered by public accountants must observe

the bylaws and rules of professional conduct in that occupation. A previous rule covered instances in which members were engaged simultaneously in the practice of public accounting and other occupations in which they rendered services of a nature similar to those rendered by public accountants. However, it was found necessary to prohibit violations of the Code by members who were not engaged in the practice of accounting, but through other organizations were rendering services of a type performed by public accountants.

Mixed Partnerships

Frequent consideration was given to the question whether it was appropriate for certified public accountants to practice in partnership with non-certified accountants. The rule against participation in professional fees by the "laity" did not seem to apply.

In 1952 the committee on ethics reported:

> The committee has under consideration the question of whether Institute members should form partnerships with non-certified accountants. It is recognized that if such a change were to be made in the rules of professional conduct, provision would have to be made for the continuation of mixed partnerships presently in existence.

However, nothing further was said on this subject until 1961, when the committee reported:

> A subcommittee has been appointed to study and submit recommendations regarding the question of mixed partnerships—that is, partnerships some of the partners of which are CPAs and some not. This is a subject which has been under consideration before and one that poses some rather difficult problems.

A major difficulty was the fact that some certified public accountants were in partnership with public accountants li-

censed under regulatory laws, who were therefore legally authorized to perform all services which CPAs were permitted to perform.

A later reference to the subject appeared in the committee's Opinion No. 6, stating that the rules did not "at present" prohibit a partnership by a member or associate of the Institute in public practice with a person who was not a certified public accountant. This view was echoed in Opinion No. 17, on "Specialization."

In any event, of course, a firm composed in part of non-certified public accountants could not use the designations "Certified Public Accountants" or "Members of the American Institute of Certified Public Accountants" in conjunction with the firm name. In many states a firm including unlicensed persons as partners could not hold itself out as practicing public accounting or express opinions on financial statements as a result of audit.

By 1964 the term "laity," in the rule prohibiting the giving or receiving of commissions or brokerages, or sharing of fees with outsiders, had raised many questions. In 1964 that term was replaced by the clause "individual or firm not regularly engaged or employed in the practice of public accounting as a principal occupation."

Employment of Lawyers

Spokesmen for the American Bar Association often complained that some accounting firms employed lawyers as members of their staffs, who were suspected of rendering legal services to the firms' clients. To prevent such illegal practice of law, an additional rule was adopted in 1957 to the effect that a member should not permit an employee to perform for the member's clients any services which the member himself or his firm was not permitted to perform.

A related question remained unsettled—whether CPAs who were also lawyers should engage in the joint practice of law and accounting. The ethics committee of the Bar Association expressed an opinion in the negative.

The National Conference of Lawyers and Certified Public Accountants took the matter under consideration. However, an organization known as the American Association of Attorney-CPAs, which included some members of the Institute and of bar associations, strongly objected to any limitation of their right to practice in both the fields in which they had become qualified. Representatives of this Association met with representatives of the Institute's ethics committee in 1967 to present their views. The ethics committee deferred consideration of the matter until other committees of the Institute concerned with the subject had reached some definite conclusion.

Responsibilities in Tax Practice

During his term as president of the Institute in the fiscal year 1956-1957, Marquis G. Eaton perceived that the rules of ethics were silent as to the responsibilities of CPAs in tax practice. He believed that relations with the Internal Revenue Service, and with the public, would be strengthened by a clarification of such responsibilities, and that the absence of such clarification by the profession itself left a vacuum which might be filled by the government or the courts.

He therefore appointed a committee on tax accounting practice, one of whose duties was stated as follows:

> To explore the possibility of devising standards of conduct for certified public accountants in tax practice which would serve as guides to members of the profession and as a protection of those who followed such standards against unjust charges of misconduct.

The first chairman of the committee was Mark E. Richardson, a partner of Lybrand, Ross Bros. & Montgomery, and a

former chairman of the Institute's committee on federal taxation. In a report to the Council in 1959, Mr. Richardson referred to the certified public accountant's reputation for independence as invaluable, and suggested that sooner or later the profession would have to determine whether the principles applicable to its auditing practice were or were not applicable to tax practice. "Most of us were quite shocked," he said, "by the questions of outstanding United States Senators at a committee hearing as to how a certified public accountant could prepare a tax return without having any knowledge of the data supporting the amounts reported therein. Similarly, concern was felt by most of us when a representative of one of the legal agencies of the government expressed a feeling that a certified public accountant's signature on a return indicated a degree of responsibility beyond that of some other preparer."

Recognizing that the rules relating to the expression of an opinion on financial statements were not intended to apply to the preparation of tax returns, Mr. Richardson said that outsiders might easily misunderstand that they did. If the profession did not clarify the position of its members in tax practice, he suggested that standards might be set by other authorities.

In response to this warning, a committee on ethics of tax practice was appointed. Several years of study ensued.

In 1962 the ethics committee published Opinion No. 13 asserting that the Code of Ethics applied to tax practice *except* those rules solely applicable to the expression of opinions on financial statements. The opinion stated specifically that the statement, affidavit, or signature of preparers required on tax returns neither constituted an opinion on financial statements nor required a disclaimer within the meaning of the Code. However, the opinion said, "In tax practice, a member or associate must observe the same standards of truthfulness and integrity as he is required to observe in any other professional work. This does not mean, however, that a member or associate may not resolve doubt in favor of his client as long as there is reasonable support for his position."

The committee on federal taxation itself, however, recognized the need for more specific delineation of the CPA's responsibilities in the various areas of tax practice. A subcommittee on responsibilities in tax practice was created, which prepared bulletins for the information and guidance of members, with the understanding that they did not have the force and effect of rules of professional conduct. Between 1964 and 1969, the tax committee issued five of these bulletins, designated as "Statements on Responsibilities in Tax Practice." The first was a description of the circumstances in which a CPA should sign a client's tax return, and the special circumstances in which his signature was not required. The second statement dealt with the CPA's responsibility when he reviewed a return of which he was not the preparer. The third statement dealt with responsibility for answering questions on tax returns. The fourth statement discussed the circumstances in which recognition should be given to an administrative proceeding of a prior year. The fifth statement dealt with the use of estimates.

This program evoked enthusiastic praise from the Internal Revenue Service.

For example, in April 1964, Mortimer M. Caplin, then Commissioner of Internal Revenue, wrote to Matthew F. Blake, who was then chairman of the subcommittee on responsibilities in tax practice: "You and your committee are to be commended for the fine work you are doing and for the contribution you are making, not only to your profession, but to the whole field of tax administration.

"All of us here are following the development of your various statements. If there is any way we can be of assistance, I hope you will call on us."

In April 1967 Fred B. Smith, General Counsel of the Treasury Department, wrote: "We applaud your efforts to streamline the techniques by which you enforce the high standards of ethical conduct of your profession. This undertaking is consistent with the Institute's impressive history of public service and responsibility."

Responsibilities in Management Services

From the earliest days of the profession, its members rendered services to clients outside the scope of auditing and tax practice. Advice and assistance in such areas as cost accounting, systems, and internal controls were commonplace. It was not until after World War II, however, that the expansion of special services seemed to require their identification as an integral part of professional accounting practice, along with auditing and taxes. "Management services," or "management advisory services" were the labels most frequently used for this purpose.

It was not until 1953, however, that an Institute committee on management services was appointed. In the following years efforts were undertaken to describe the role and responsibilities of CPAs in this field, where the nature of the work differed from that of auditing and tax practice.

The relationship of management services and audit independence has been discussed at length in Chapter 8, including reference to Opinion No. 12 of the ethics committee, holding that no necessary conflict of interest existed if decision-making was avoided.

While considering the applicability of the Code of Ethics to tax practice, the ethics committee also decided in its Opinion No. 14 that the Code applied to management advisory services with the exception of those rules solely applicable to expressions of opinions on financial statements.

With specific reference to management advisory services, the ethics committee issued Opinion No. 17 in 1964, to the effect that a member might form a separate partnership with non-CPA specialists in management services, provided such partnership observed the profession's Code of Ethics. This opinion was supported by extensive discussion but concluded by emphasizing that it was based on the Code of Ethics as then constituted: "If the provisions in question are revised, it may be necessary to modify or withdraw this opinion."

In 1969 the Institute's committee on management services

issued its first three "Statements on Management Advisory Services." The first was a description of the nature of management advisory services by independent accounting firms. The second discussed competence in management advisory services. The third described the role of CPAs in performing such services. The first statement contained the admonition that an independent accounting firm in providing management services must give particular consideration to both independence and the *appearance* of independence as set forth in the Code and in Opinion No. 12 of the ethics committee. The statement also referred to Opinion No. 14, cited above. In Statement No. 2 on "Competence," the general standard was postulated:

> In all matters relating to a management advisory services assignment, an independence in mental attitude is to be maintained by the member and his staff.

Similar admonitions appeared in Statement No. 3, among them the following:

> The nature and objectives of such engagements are analogous to audit services in the sense that an impartial, objective judgment is being sought by the client.

It seemed likely that in due course the committee on management services would follow the example of the tax committee in publishing statements specifically describing the ethical responsibilities of CPAs in various aspects of management advisory services.

What has been recited in this chapter is ample evidence of the profession's determination continually to raise its ethical standards. Increasing responsibilities were accepted, and good faith was shown in enforcing compliance with the standards. With few exceptions the progress was made at the initiative of the profession itself.

In practice there was no comparison between the level of

conduct observed in 1969 and that of even 30 years before. The improvement was dramatic. The evidence suggests that it was largely through the elevation of its ethical standards that the profession maintained the authority with which public acceptance invested it—the authority to discipline itself, to continue its customary tax practice, and to influence the financial reporting of the nation's business enterprises. The acceptance of ever greater responsibility evoked praise from government agencies, the banking community, investors, and others concerned. Despite disagreement over specific issues, and occasional setbacks, progress was steady and promised to continue.[1]

---

[1] Following are the names of the chairmen of the Institute's committee on professional ethics from 1937 to 1969, who were largely responsible for the progress described in this chapter:

Philip N. Miller	1936-1937	Samuel W. Eskew	1950-1951
I. Graham Pattinson	1937-1939	Edward J. McDevitt	1951-1954
George Cochrane	1939-1940	George A. Hewitt	1954-1955
Frederick H. Hurdman	1940-1942	Frank L. Wilcox	1955-1958
Joseph J. Klein	1942-1944	Thomas G. Higgins	1958-1960
Homer N. Sweet	1944-1945	Richard S. Chamberlain	1960-1962
Donald M. Russell	1945-1948	John R. Ring	1962-1964
Earl A. Waldo	1948-1949	Ralph S. Johns	1964-1967
John H. Zebley, Jr.	1949-1950	Thomas D. Flynn	1967-1969

In recent years Donald Schneeman, director of professional ethics, has contributed substantially to the successful discharge of the committee's rapidly increasing responsibilities.

CHAPTER 18

Planning for the Future

SOON after his election as president of the Institute in the fall of 1956, Mark Eaton appointed a committee on long-range objectives. In his report to the membership at the close of his term of office, Mr. Eaton explained the reasons for this appointment as follows:

> Professional accountancy has never defined its course of direction. We have not decided whether the CPA certificate is minimum or maximum equipment—whether the professional accountant should be expected to reach much further with his abilities than is indicated by the CPA certificate. We have never decided whether management services should be the common practice of all accounting offices, or of only a few. We have never described the level at which we should discharge our public responsibilities—whether only at the technical level or whether also at the policy level. We have not taken formal action to decide, on reasoned grounds, whether the Institute itself is an organization of CPAs in public practice, or an organization of CPAs no matter how employed. A long list of such unsettled questions could be compiled.
>
> It is a commonplace of business management to state the general objectives, and to agree upon long-range and short-range plans. With this kind of information in hand it is possible to build the necessary types of organization, to fix responsibilities, to allocate resources,

and, most important of all, to make intelligent choices between alternatives—choices for both the long-range and the short-range.

A committee on long-range objectives has, therefore, been created this year to tackle a part of this problem. At my request it addressed itself first to the question whether the Institute should endeavor to eliminate existing distinctions between members in public practice and members who are not.

Identifying Long-Range Objectives

The personnel of this first committee on long-range objectives was selected with great care. J. S. Seidman, senior partner of Seidman & Seidman, was named chairman. He was known as a thorough and tireless worker, a creative and sometimes unconventional thinker, and a man who was dedicated to the progress of his profession. The second member was Herman W. Bevis, senior partner of Price Waterhouse & Co., who had served with distinction as chairman and member of many Institute committees, and was deeply involved intellectually with many of the profession's problems. The third member was Robert E. Witschey, head of his own local firm in Charleston, West Virginia, which he had founded after his service with the Navy in World War II, only 12 years before. The firm had flourished, however, and Mr. Witschey had become widely known as a student of the profession's problems and an articulate spokesman for the local accounting firms and individual practitioners.

The committee had been limited to three members in order to facilitate close collaboration and intensive discussion.

Status of Members Not in Practice

The assignment on which President Eaton had asked this committee to "cut its teeth" had been deliberately selected as a relatively simple one—whether the Institute was an organiza-

tion of CPAs in public practice or an organization of CPAs no matter how employed.

Since the planning process was new to the Institute, there were no procedural precedents. To begin with, the committee reviewed procedures followed by corporate managements. One model was the General Electric Company, which had spent much time and money in planning, and whose officers had published the results in some detail.

The committee then addressed itself to the specific question before it. The policies of other professional organizations in the United States were investigated, as well as those of other accounting organizations abroad. Armed with the accumulated information, the committee "brain-stormed" the problem at all-day or two-day meetings, which were usually held in the seclusion of a hotel suite or a club.

Even in this small group, however, differences of opinion developed. In its first report to the Council, in 1957, the differing points of view were presented, together with an analysis of the Institute's present policies, how these policies were arrived at, how the present membership was constituted, and how other organizations had dealt with the same question.

The committee was unanimous in the conclusion that CPAs not in practice should continue to be eligible for membership in the Institute. However, one member believed that the Council, the executive committee, the Board of Examiners, the Trial Board, and other committees dealing with internal government, such as those on nominations and admissions, should continue to be composed solely of CPAs in practice. The other two members of the committee believed that all members should have equal opportunities in the Institute.

The Council discussed the question, but deferred final action until its spring meeting in April 1958. There, after further debate, the following statement of objective was adopted:

> It is an objective of the Institute to serve as the national organization of certified public accountants in and out of public practice, and to develop and maintain the form of organization best adapted to the needs of all its members.

It had taken a year and a half to reach this somewhat inconclusive result. Nevertheless, the impact was significant. This general statement of policy led to changes in the bylaws which ultimately admitted to the Council members engaged in industry, in teaching, and in government. Representatives of all three groups were also admitted to senior committees of the Institute. It became a custom to elect at least one industrial accountant and one professor of accounting as members of the powerful executive committee.

Only a few exclusions were retained. The six officers of the Institute—president, vice-presidents, and treasurer—were required to be members in practice. The Trial Board was composed entirely of members in practice, as was the committee on admissions. Otherwise, the opportunities for activity and advancement in the Institute were open to all members.

This liberalization of former policies markedly strengthened the relations between Institute members in and out of practice. The latter had given evidence of some discontent with their apparently second-class status. A by-product was better relations with accounting organizations representing industrial accountants, to which many non-practicing members of the Institute belonged.

These effects of adoption of the objective were salutary, but the Institute also gained much from the ability to utilize the talents and experience of members who had proven themselves in the industrial, academic, or governmental worlds.

The advantages as well as the difficulties of systematic planning had been demonstrated.

With enthusiasm, the committee on long-range objectives turned its attention to a second project.

Relations With Other Organizations

This was the question of the appropriate relationships of the Institute with other organizations interested in accounting, such

as the national organizations of accounting educators, controllers, and industrial and governmental accountants.

To expedite production, the committee decided that each topic selected for study would be assigned to one of the committee members, who would write a paper providing background information and analyzing the problem to which an answer was sought. The whole committee would review drafts of the paper and decide what changes should be made and what conclusion should be recommended. The final draft would be published for general information before the Council was asked to adopt a policy position on the problem.

The Institute's relations with other accounting organizations could not be developed intelligently, in the committee's opinion, without first answering the question, "What is accounting and where is it going?" Herman Bevis was asked to tackle this question. The result was his classic paper, "The Accounting Function in Economic Progress," published in *The Journal of Accountancy* for August 1958. The conclusion was, "Accounting is not merely a contributor to economic progress, it is an inherent part of a successful industrialized economy, indispensable to a high degree of efficiency in an organization with a complex management problem. The accounting function in the United States is discharged not by one but by many groups of persons whose activities interrelate."

On the basis of this paper the committee recommended, and the Council adopted, the following objective in October 1958:

> It is an objective of the Institute to encourage co-operation and consultation among national organizations of accountants to the end that the entire accounting function may make its greatest contribution to the public welfare.

This policy statement was implemented in various ways. Meetings of leaders of the representative national organizations were held periodically. Members of the staffs, such as executive directors and research directors, exchanged views on matters of common interest and information on how each organization was approaching related problems. Relations among the groups,

which theretofore had been casual and sporadic, became much more purposeful, and duplication of effort and expense was minimized.

Encouraged by these successes, the committee on long-range objectives extended the scope of its activity. It arranged meetings in different parts of the country, where it could confer with representatives of state societies of certified public accountants. New subjects for consideration were added to the agenda. The committee members were busy with research and writing. Bob Witschey produced a paper on "The Accounting Function for Small Business," and Jack Seidman on "What is the Future of the Accounting Profession?"

Changes in Personnel

In 1959 Mr. Seidman became president of the Institute. The chairmanship of the committee on long-range objectives passed into the hands of Herman Bevis. Bob Witschey retired after three years of service. In the previous year, Robert M. Trueblood had been named as a fourth member of the committee. Norton M. Bedford, professor of accounting at the University of Illinois, and Clifford V. Heimbucher, who has been frequently mentioned in these pages, were added to the committee.

Mr. Trueblood had attracted attention as an original and creative thinker and a highly articulate speaker and writer. He was then a partner in charge of the Pittsburgh office of Touche, Ross, Bailey & Smart. He had served as president of the Pennsylvania Institute of Certified Public Accountants.

Mr. Heimbucher, thoughtful and widely read, was also peculiarly well fitted for this committee. He had gone through the chairs of the California Society of Certified Public Accountants, including the presidency, and had served with distinction on a number of Institute committees. Norton Bedford was regarded as a highly promising younger member of the

academic community, an original thinker, a facile speaker and writer.

In 1961, Mr. Bevis retired from the committee after five years of service. Bob Trueblood assumed the chairmanship for the next four years, and Malcolm M. Devore of Haskins & Sells was added to the committee. When Cliff Heimbucher became president of the Institute in 1963, David F. Linowes took his place as a member of the committee. Mr. Linowes had been head of his own local firm in Washington, D.C. but at that time had become a partner of S. D. Leidesdorf & Company in New York. He, too, had attracted attention as an original thinker and a prolific speaker and writer. He later became treasurer and then a vice president of the Institute. Bob Trueblood was elected president in 1965.

Successes and Defeats

In the period ended in 1962 the following members of the committee produced additional papers. "Professional and Technical Practitioners in Accounting" (Trueblood), "The Management Service Function in Public Accounting" (Trueblood), "Fifty-three Jurisdictions" (Heimbucher), "Education for Accounting as a Learned Profession" (Bedford), and "The CPA's Attest Function in Modern Society" (Bevis).

Seven additional objectives recommended by the committee had been adopted by the Council. All the committee's recommended objectives were thereafter reprinted in the successive pamphlets containing the Institute's bylaws and Code of Ethics, which were sent to all members.

The committee was not always successful. In 1960 the Council approved the objective that ultimately members of state societies and of the Institute be required to be members of both. Amendments to the bylaws designed to accomplish this objective failed to pass when submitted for vote by a mail ballot to

the entire membership in 1964. The failure was attributed to concern on the part of state societies that the Institute might acquire control over them, although the proposal was limited to mandatory concurrent membership, without affecting the independence of either the national or the state organizations.

Again, in 1962, the committee proposed as an objective that advanced study and superior attainment be formally recognized in order to encourage continuous study and self-improvement on the part of CPAs. The proposed mechanism for attainment of this objective was an "Academy of Accountancy," similar to the College of Physicians and Surgeons in the medical profession. The debate in the Council resulted in rejection of this proposal. Several reasons were indicated: one, concern on the part of local practitioners that the personnel of national firms would more readily gain recognition of superior attainment; another, that the CPA certificate would be downgraded; and a third, that too many "charter members" of the proposed academy were suggested for admission without any formal tests.

"Where Is It Headed?"

In 1962 the Institute published a monograph entitled *The Accounting Profession—Where Is It Headed?* which summarized the views on the profession's future reflected in the long-range committee's papers of the preceding six years. The monograph was edited by the Institute's executive director and copies were sent without charge to all firms represented in the Institute. Many additional copies were sold.

This publication had a visible influence on the thinking of the profession. State societies undertook similar planning activities. Some accounting firms began to consider formal planning procedures. Quotations from the monograph appeared in articles and speeches for years thereafter.

A New Approach

Under the leadership of Robert Trueblood, the committee decided to embark on another course. The work of the preceding years had established objectives related to basic internal problems of the profession, including relations with non-practicing members, other accounting organizations, non-certified accountants, and state societies; the CPAs' practice in management services; technical competence; extension of the attest function, and requirements for the CPA certificate. However, not much attention had been given to the profession's problems in adapting to the rapidly changing environment. The committee undertook to examine the forces at work which would influence the profession's development in the years ahead and to try to identify the problems which might emerge.

As a beginning, a working paper was prepared entitled, "Profile of the Profession: 1975," which consisted of a lengthy series of questions, filling 58 double-spaced typewritten pages and arranged under the following subject headings:

1. The environment
2. Areas of professional service
3. Problems of education
4. Research attitudes and problems
5. Professional ethics and the ethics of practice
6. Personnel—procurement and retention
7. Public interest and social obligation
8. Structure of the profession.

This paper was distributed to state societies and to interested members of the Institute, with a request for their views on any or all of the questions.

Next, conferences were arranged with individual consultants who were knowledgeable in the subject matter covered by these questions. Some of the consultants were CPAs, but most were experts in other areas. Some of the conferences lasted a full

day, others a half day, and in some cases two or three consultants on a common problem were interviewed at the same time. The conversations were informal and unstructured. Stenographic transcripts were made by a court reporter. A member of the committee was asked to prepare a "position working paper" based on the transcript of each discussion. These working papers were sent to all officials of the Institute and to state societies, and were offered to members on request, with an invitation to comment.

In the course of this work, a number of meetings were held with individual practitioners, state society executives, American Institute staff members, and others whose views were solicited on the questions under consideration.

Altogether, between 1961 and 1965 formal consultations, of which a record was made, were held with 29 individuals, including a behavioral scientist, two mathematicians, a political scientist, a sociologist, an economist, a non-accountant dean of a graduate school of business, three distinguished accounting professors, the chairman and the chief accountant of the Securities and Exchange Commission, a former commissioner of Internal Revenue, the presidents of two corporations—one large and one small—a public-relations consultant, the head of an investment-banking firm, a vice president of a large metropolitan commercial bank, a financial analyst, five distinguished accountants from outside the United States, a partner of a large law firm, three CPAs, each of whom specialized in one area of practice, and a distinguished generalist, John W. Gardner, then president of the Carnegie Corporation.

The committee then asked the executive director of the Institute to summarize the results of all these discussions in a book which might help the Institute, the state societies, and accounting firms and practitioners in their own planning efforts. The result was *The CPA Plans for the Future,* published by the Institute in 1965.

More than 12,000 copies of this book were distributed. It was reviewed in many accounting periodicals. A few professors of accounting required their advanced students to read it. It was

frequently quoted in speeches and articles. It was also used as a model for planning in other organizations, some of them entirely unrelated to accounting.

This book, however, marked only one step in the planning process. It did not recommend specific solutions of the profession's problems: it only identified the problems and provided background for consideration of possible alternative solutions. In a foreword, Clifford V. Heimbucher, then president of the Institute, explained its purpose. The book, he said, had been published "in the belief that candid discussion of the problems which confront the accounting profession, and of alternative paths for development in the future will assist in early and sound solutions and decisions." He explained that the book did not represent official policies of the Institute, and that many of the senior committees would disagree with some of the ideas presented: "The principal purpose of the book is to provoke thought and debate while peering into the future. Even if some of the problems the author has conceived turn out to be imaginary, it will do no harm to consider and dispose of them and, in the process, hopefully to develop other constructive ideas."

There was another important by-product of the long-range committee's work. Robert Trueblood personally prepared a record of the committee's activities over the ten-year period, which, together with all the official papers prepared under the committee's auspices, was bound in two large volumes. Copies were presented—in many cases at formal meetings—to deans or senior faculty of hundreds of universities, where the volumes were made available for research and reference.

Planning for the Profession

What to do next? The executive committee concluded that the work already done provided a basis for specific planning for solution of the problems identified in *The CPA Plans for*

the Future. In order to stimulate interest in the planning process, small seminars were held in various parts of the country to discuss the future of the profession. In a report to the Council, the executive committee said: "If the problems in the book are studied solely by small committees, their recommended solutions may seem so radical or novel that they will be rejected or ignored. It seems desirable, therefore, to encourage the broadest possible discussion of the problems which the book identifies, and to elicit from these discussions agreement or disagreement with various solutions which may be proposed."

A new committee was appointed, designated as the "planning committee," whose job it would be to sift all the information and opinion available and develop action programs to achieve the profession's objectives.

The planning committee consisted at first of seven of the younger members of the profession, five of them under 45 years of age. The chairman was Gordon Ford, senior partner of the firm of Yeager, Ford & Warren, Louisville, Kentucky.

Formal seminars on *The CPA Plans for the Future* were held in 1965 and 1966, most of them two days in length. Two seminars occurred in New York, and others in Chicago, Urbana, Philadelphia, San Francisco, Washington, D.C., Louisville, Cleveland, and Princeton. Meetings of state societies or their chapters were held in 27 states for similar discussions. Two regional conferences held in the spring of 1966 included sessions devoted to discussion of specific problems outlined in the book.

Records of most of these discussions were made available to the planning committee, which then began the task of developing specific recommendations.

First it decided that a description of the nature of public accounting practice was essential for intelligent consideration of all additional problems. The next step was to select from among the multitude of questions which might be examined those which the committee believed had the highest priority.

At the first two meetings, agreement was reached on the

questions which the committee would tackle first. These were listed in an agenda consisting of nine major questions, under each of which were a number of specific related questions. The major topics were the nature of the professional practice of accounting, standards of competence, personnel requirements, standards of performance and conduct, the impact of computers, the implications of the firm as the unit of practice, public relations, research requirements, and the role of the Institute, the state societies, state boards, firms, and individual members in delineating and implementing the profession's objectives.

For the next year the committee devoted most of its attention to the preparation of the "Description of the Professional Practice of Accounting by Certified Public Accountants," which after exposure and revision was approved by the Council. This short description was published for the information of all members, and was also widely distributed in the academic community and among other interested groups. (It was quoted in full in the first chapter of Volume I of this work.) It was the first authoritative statement of the nature and scope of the public practice of accounting.

Thereafter the planning committee developed recommended programs for specific action in the areas of public relations, education for certified public accountants, research in accounting, and attraction of personnel to public accounting firms. After approval by the executive committee, these programs were published in *The Journal of Accountancy*. The recommendations were incorporated in the Institute's annual plans for its own activities.

The work of the planning committee was expected to continue indefinitely. New topics were added to its agenda each year.

Planning for the Institute

While the planning committee was examining the problems of the profession as a whole, Robert Trueblood, who as presi-

dent of the Institute had not lost his interest in systematic planning, appointed a "committee on structure" to study the organization and procedures of the Institute itself. This three-man committee was also selected with great care, consisting of James VanderLaan, partner of Collins, Peabody, Masters & VanderLaan, Denver, as chairman; Walter J. Oliphant, managing partner of Arthur Andersen & Co., Chicago; and Kenneth Axelson, vice president of J. C. Penney & Co., New York. A management consultant, Robert Greenleaf, was engaged to assist this new committee, and John Lawler, managing director of the Institute, provided staff assistance.

The committee's charge was to review the Institute's organization, decision-making processes, and operating mechanism —to determine whether improvements could be made which would enable the Institute to serve the needs of the profession effectively in the years ahead.

By questionnaire and interview, the committee consulted a large cross-section of the Institute's membership and members of its staff. It analyzed the committee and staff structure, reviewed the financial and administrative controls, and in particular, studied the processes by which decisions were made —or not made. Frequent meetings were held, at which the members of the committee debated possible improvements in all these areas.

The committee's report was approved, with the exception of one recommendation, at the meeting of Council in May 1966, and was published for the information of all the members on August 10 of that year. Copies were sent to all members of the Institute.

A number of weaknesses in the Institute's organization and decision-making processes were disclosed. The committee concluded that the Institute had recently passed over the line that separated a small from a large organization—not only in sheer size, but also in complexity of program—but that the structure and procedures of the Institute had not been fully adapted to the change.

The report suggested that the Institute's basic objective

was to be a "distinguished institution, a pace-setter among professional societies." To achieve this, it was considered necessary for members to expand their participation in its work and for the staff to be substantially strengthened.

The committee proposed eight major goals. It then recommended a strengthening of the executive office and the technical staff, assumption of greater responsibilities by the executive committee, and decentralization of responsibility for decision-making and action under general policy supervision.

Under instructions of the executive committee, the executive director of the Institute then prepared a series of papers containing detailed recommendations for organizational changes consistent with the structure committee's conclusions. After extensive discussion and exposure to the Council, many of these recommendations were included in a complete revision of the Institute's bylaws approved by the membership by mail ballot in 1969. Other recommendations, not requiring bylaw changes, were implemented by executive order.

The principal changes were, in brief, as follows:

- The executive committee was enlarged and constituted as a Board of Directors, with overall responsibility, subject to the veto of the Council, for policies and activities of the entire organization.

- A full-time executive vice president was appointed, in the person of a certified public accountant responsible for co-ordination of all the technical activities of the Institute and authorized to act as spokesman for the Institute. The occupant of this position was Leonard M. Savoie, formerly a partner of Price Waterhouse & Co., who had served on many committees of the Institute, including the planning committee, and had participated as a consultant in the work of the Accounting Principles Board. He was thoroughly familiar with the problems of the Institute in the technical areas, and his own professional reputation clothed him with a high degree of personal authority. At the same time, the executive director of the Institute,

John L. Carey, was given the title of administrative vice president, with responsibility for administration of the staff organization, and co-ordination of its work in the non-technical areas. His retirement date, however, was May 1, 1969, and he was succeeded in the position of administrative vice president by John Lawler, who had been a member of the Institute's staff for some 20 years, serving in its public-relations department, as co-ordinator with state societies, as editor of *The Journal of Accountancy,* as deputy executive director and as managing director. Both the executive and administrative vice presidents were made ex officio members of the executive committee, or, as it soon became, the Board of Directors.

• The work of the Institute was assigned to a number of major "divisions," incorporating both senior committees and related staff. The senior committees became, in effect, executive committees of the divisions. The staff directors, with their assistants, were to work with their executive committees, and related committees, much as the executive director in previous years had worked with the executive committee and related committees. Decentralization of decision-making and closer co-ordination of committee and staff work were the expected results, all under the supervision of the Board of Directors and the ultimate control of the Council.

• Formal planning procedures were instituted: each division submitted to the executive and administrative vice presidents activity programs proposed for the ensuing year based, where appropriate, on the planning committee's recommendations. With the assistance of the controller of the Institute, the administrative vice president, in consultation with the executive vice president, modified the plans as necessary in the light of the budgetary limitations, and submitted an overall planning document to the Board of Directors for approval.

As Mr. Lawler reported on the planning process to the Council in 1968:

> A prudent allocation of our resources involves three steps. The first of these is the selection of long-term goals for the organization—we now have a fairly complete set of them. The second is the assembly and utilization of reliable estimates of the anticipated costs for every major project or activity—and we now have such information available to us. And the third is the inauguration of systems analysis to produce some objective evidence of the benefits derived or anticipated from any substantial expenditure—and we lack that kind of data in many crucial areas. In the absence of it, the task of making selections among a vast array of alternative uses for the Institute's funds can be an extremely troublesome one.

It was recognized that selection of program priorities involved a high degree of subjective judgment, but that even subjective judgment, based on a careful analysis of goals, immediate problems, and financial resources available, could result in far more useful plans than an unco-ordinated program and budget, reflecting only the requests of individual committees and staff members.

The goals, to which Mr. Lawler referred, were adopted in 1968 by the executive committee and approved by the Council, combining the objectives recommended by the original committee on long-range objectives, the eight major goals proposed by the committee on structure, and other decisions of the executive committee and the Council itself. The following official statement, while subject to modification and amplification in the light of changing conditions, served as a focal point for all planning:

Objectives of the American Institute of Certified Public Accountants

1. To sustain itself as an organization of distinction by the wide participation of its members, by the intensive creative

involvement of the best of the profession in Institute affairs, and by an exceptional quality of staff performance.

2. To adopt a form of organization best designed to meet the needs of all its members both in and out of practice.

3. To engage a full-time staff of sufficient size and competence and to organize their efforts—both in terms of direct staff work and assistance to committees—so that the organization can move with speed and precision to strengthen continually its service and its leadership.

4. To perform in a manner which will persuade all the parties at interest—government, financial institutions, the business community, universities, and the public generally—to accept the organization as the authoritative source of principles and procedures in its field.

5. To promote improvements in financial reporting by seeking to eliminate variations in reporting practices which are not justified by substantial differences in circumstances.

6. To communicate effectively to the public, as well as to all levels of government, in regard to matters of concern to the profession.

7. To produce valuable new knowledge in its field through research and experimentation, the analysis and synthesis of experience, and the development and adaptation of new techniques.

8. To identify those areas in society where the need for the CPA's attest function exists and to assist its members in equipping themselves to perform the attest function wherever a useful social purpose would be served.

9. To maintain surveillance over practice in the interest of promoting high standards of performance by the profession and public confidence in its work.

10. To promote the adoption of uniform nationwide standards governing the issuance of CPA certificates, recognition of qualified accountants of other countries, and freedom of movement in interstate and international accounting practice.

11. To serve as a constructive force in improving education for the profession and, ultimately, all business education.

12. To encourage a continuous restatement of those areas of knowledge and technical competence required by the CPA in his present and prospective practice, and a clarification of the responsibility appropriate to universities, practitioners and professional societies in the education and training of CPAs.

13. To maintain a high level of quality in its publications and in its program of professional development, and thus to aid its members in discharging their commitment as professional men to a lifetime of study and self-improvement.

14. To co-ordinate on a voluntary basis the plans, programs, and activities of the state societies and of the Institute, with particular emphasis on the adoption of uniform codes of professional ethics and enforcement procedures.

15. To co-operate fully with all organizations of accountants, both at home and abroad, to the end that the entire accounting function can make its maximum contribution to the public good.

16. To encourage every eligible CPA, in furtherance of his personal development and in fulfillment of his professional obligations, to become a member of both his state society and the Institute.

17. To encourage all CPAs to perform a wide range of services in the broad field of accounting consistent with their professional competence and their ethical responsibilities. [Here reference was made to the "Description of the Professional Practice of Accounting by Certified Public Accountants."]

Conclusion

This summary of the Institute's planning efforts seems an appropriate conclusion to the story of the rise of the accounting profession in the United States. The character and temper of the certified public accountants are accurately reflected in the 13 years of intensive work so briefly outlined in this final

chapter. The results show clearly that large numbers of thoughtful, intelligent, high-minded, energetic, and able men were deeply concerned about their role in society and their opportunities for service. Their goals were inspiring. The organization and procedures adopted to achieve the goals were superior to those of the vast majority of similar organizations. The time, energy, and money which thousands of certified public accountants freely contributed to the development of their profession was impressive evidence of their dedication.

The accounting profession, when viewed in the perspective of the 80-odd years since its beginnings in this country, appears as a body of men possessed of amazing vitality, an extraordinary capacity for self-criticism, an ability to act effectively on many broad fronts, and a determination to render constructive service to the society of which they are a part.

Appendix A

Officers of the American Institute of Accountants and American Institute of Certified Public Accountants to 1969

American Institute of Accountants

Officers

1936-1937

President	Robert H. Montgomery
Vice-presidents	Charles F. Rittenhouse
	Edwin H. Wagner
Treasurer	Arthur W. Teele
Secretary	John L. Carey

1937-1938

President	Clem W. Collins
Vice-presidents	William C. Heaton
	Anson Herrick
Treasurer	Arthur W. Teele
Secretary	John L. Carey

1938-1939

President	Clem W. Collins
Vice-presidents	Lewis Ashman
	John K. Mathieson
Treasurer	Arthur W. Teele
Secretary	John L. Carey

1939-1940

President	John K. Mathieson
Vice-presidents	Samuel J. Broad
	Lincoln G. Kelly
Treasurer	Arthur W. Teele
Secretary	John L. Carey

1940-1941

President	C. Oliver Wellington
Vice-presidents	Maurice E. Peloubet
	T. Dwight Williams
Treasurer	Samuel J. Broad
Secretary	John L. Carey

1941-1942

President	Norman L. McLaren
Vice-presidents	George Cochrane
	George S. Olive
Treasurer	Samuel J. Broad
Secretary	John L. Carey

1942-1943

President	George S. Olive
Vice-presidents	George P. Ellis
	Victor H. Stempf
Treasurer	Samuel J. Broad
Secretary	John L. Carey

1943-1944

President	Victor H. Stempf
Vice-presidents	George D. Bailey
	J. A. Phillips
Treasurer	Samuel J. Broad
Secretary	John L. Carey

1944-1945

President	Samuel J. Broad
Vice-presidents	Rodney D. White
	Edward B. Wilcox
Treasurer	Maurice E. Peloubet
Secretary	John L. Carey

1945-1946

President	T. Dwight Williams
Vice-presidents	Homer N. Sweet
	Earl A. Waldo
Treasurer	Maurice E. Peloubet
Secretary	John L. Carey

1946-1947

President	Edward B. Wilcox
Vice-presidents	Parry Barnes
	Percival F. Brundage
Treasurer	Maurice E. Peloubet
Secretary	John L. Carey

1947-1948

President	George D. Bailey
Vice-presidents	Ralph B. Mayo
	J. Harold Stewart
Treasurer	Charles H. Towns
Secretary	John L. Carey

1948-1949

President	Percival F. Brundage
Vice-presidents	T. Coleman Andrews
	J. William Hope
Treasurer	Charles H. Towns
Executive Director	John L. Carey

1949-1950

President	J. Harold Stewart
Vice-presidents	Maurice Austin
	George O. Carlson
	James I. Keller, Jr.
	Maurice H. Stans
Treasurer	Warren W. Nissley
Executive Director	John L. Carey

1950-1951

President	T. Coleman Andrews
Vice-presidents	Gordon S. Battelle
	Richard C. Mounsey
	Frank L. Wilcox
	John H. Zebley, Jr.
Treasurer	Harold R. Caffyn
Executive Director	John L. Carey

1951-1952

President	J. William Hope
Vice-presidents	Marquis G. Eaton
	Arthur B. Foye
	George E. Perrin
	Donald M. Russell
Treasurer	Harold R. Caffyn
Executive Director	John L. Carey

1952-1953

President	J. A. Phillips
Vice-presidents	Thornton G. Douglas
	Samuel W. Eskew
	Coleburke Lyons
	Mark E. Richardson
Treasurer	Harold R. Caffyn
Executive Director	John L. Carey

1953-1954

President	Arthur B. Foye
Vice-presidents	M. C. Conick
	James E. Hammond
	Wallace M. Jensen
	John A. Peyroux, Jr.
Treasurer	William M. Black
Executive Director	John L. Carey

1954-1955

President	Maurice H. Stans
Vice-presidents	Ira N. Frisbee
	Alvin R. Jennings
	John C. Martin
	Virgil S. Tilly
Treasurer	William M. Black
Executive Director	John L. Carey

1955-1956

President	John H. Zebley, Jr.
Vice-presidents	Dixon Fagerberg, Jr.
	John A. Lindquist
	J. S. Seidman
	Robert E. Witschey
Treasurer	William M. Black
Executive Director	John L. Carey

American Institute of Certified Public Accountants

Officers

1956-1957

President	Marquis G. Eaton
Vice-presidents	William S. Deeming
	L. H. Penney
	Donald P. Perry
	R. Warner Ring
Treasurer	John B. Inglis
Executive Director	John L. Carey

1957-1958

President	Alvin R. Jennings
Vice-presidents	Donald J. Bevis
	Roy C. Comer
	Louis H. Pilie
	John M. Stoy
Treasurer	John B. Inglis
Executive Director	John L. Carey

1958-1959

President	Louis H. Penney
Vice-presidents	William P. Hutchison
	Hugh M. Mercer
	Robert J. Murphey
	John W. Queenan
Treasurer	Thomas D. Flynn
Executive Director	John L. Carey

1959-1960

President	J. S. Seidman
Vice-presidents	Frank L. Arnold
	Russell S. Bock
	Edward J. McDevitt
	Hatcher A. Pickens
Treasurer	Thomas D. Flynn
Executive Director	John L. Carey

1960-1961

President	Louis H. Pilie
Vice-presidents	Herman W. Bevis
	Clifford V. Heimbucher
	Homer L. Luther
	Edwin W. Norberg
Treasurer	Thomas D. Flynn
Executive Director	John L. Carey

1961-1962

President	John W. Queenan
Vice-presidents	Richard L. Barnes
	Richard S. Claire
	Thomas D. Flynn
	Marvin L. Stone
Treasurer	Roger Wellington
Executive Director	John L. Carey

1962-1963

President	Robert E. Witschey
Vice-presidents	Hilliard R. Giffen
	Chris H. King
	David F. Linowes
	Robert M. Trueblood
Treasurer	Roger Wellington
Executive Director	John L. Carey

1963-1964

President	Clifford V. Heimbucher
Vice-presidents	William H. Holm
	J. T. Koelling
	J. Earl Pedelahore
	William J. von Minden
Treasurer	Roger Wellington
Executive Director	John L. Carey

1964-1965

President	Thomas D. Flynn
Vice-presidents	Horace G. Barden
	Maurice J. Dahlem
	Bernard B. Isaacson
	John R. Ring
Treasurer	David F. Linowes
Executive Director	John L. Carey

1965-1966

President	Robert M. Trueblood
Vice-presidents	Malcolm M. Devore
	Claude M. Hamrick, Jr.
	Gerald C. Schroeder
	James VanderLaan
Treasurer	David F. Linowes
Executive Director	John L. Carey

1966-1967

President	Hilliard R. Giffen
Vice-presidents	George D. Anderson
	John P. Goedert
	Ralph E. Kent
	E. C. Leonard, Jr.
Treasurer	David F. Linowes
Administrative Vice-president	John L. Carey

1967-1968

President	Marvin L. Stone
Vice-presidents	Durwood L. Alkire
	Samuel A. Derieux
	Eli Mason
	Walter J. Oliphant
Treasurer	Ralph E. Kent
Past President	Hilliard R. Giffen
Administrative Vice-president-Secretary	John L. Carey
Executive Vice-president	Leonard M. Savoie

1968-1969

President	Ralph E. Kent
Vice-presidents	Walter M. Baird
	Elmer G. Beamer
	Paul Lambert, Jr.
	Stanley J. Scott
Treasurer	Walter E. Hanson

Past President	MARVIN L. STONE
Administrative Vice-president-Secretary	JOHN LAWLER
Executive Vice-president	LEONARD M. SAVOIE

1969-1970

President	LOUIS M. KESSLER
Vice-presidents	MARSHALL S. ARMSTRONG
	WINSTON BROOKE
	STANLEY D. FERST
	KENNETH L. THOMPSON
Treasurer	WALTER E. HANSON
Past President	RALPH E. KENT
Administrative Vice-president-Secretary	JOHN LAWLER
Executive Vice-president	LEONARD M. SAVOIE

Appendix B

Gold Medal Award Winners

In 1944 the Institute established an award, in the form of a gold medal, with citation, for distinguished service to the profession, including notable contributions to accounting literature. Following are the names of the gold medal winners in the succeeding 25 years:

1944 J. Harold Stewart
George Oliver May
William A. Paton
1945 Victor H. Stempf
E. L. Kohler
W. W. Cooper
1946 Arthur H. Carter
Maurice E. Peloubet
1947 T. Coleman Andrews
1948 Edward A. Kracke
N. Loyall McLaren
1949 Hiram T. Scovill
Robert H. Montgomery
1950 (No Award)
1951 (No Award)
1952 Samuel J. Broad
Percival F. Brundage
1953 Carman G. Blough
Mark E. Richardson
1954 Maurice H. Stans
1955 Saul Levy
Lloyd Morey
1956 J. S. Seidman
1957 William B. Franke
Arthur B. Foye
Donald P. Perry
1958 Marquis G. Eaton
1959 Paul Grady
1960 George D. Bailey
1961 John L. Carey
J. A. Phillips
1962 Alvin R. Jennings
1963 (No Award)
1964 Thomas W. Leland
Andrew Barr
1965 Thomas G. Higgins
1966 Louis H. Penney
1967 Clifford V. Heimbucher
Robert E. Witschey
1968 John W. Queenan
1969 Herman W. Bevis

Index for Volumes I and II

Index

Volume numbers are indicated by boldface

"Abuse of the Audit in Selling Securities, The" (Smith), **1**:77-78
Academia, pressure for comparability, **2**:70-71
"Academic Preparation for Professional Accounting Careers," **2**:282, **2**:283
"Academy of Accountancy," **2**:492
Academy of Professional Accounting, **2**:338
"Acceptability of Commercial Paper," **1**:293
"Accountancy Is a Career for Educated Men," **1**:276, **2**:262-263, **2**:305
Accountancy laboratory (Columbia), **1**:99, **1**:170
Accountancy legislation, restrictive, **1**:282-286
Accountancy Publishing Company, **1**:100, **1**:101
Accountant (s)
- concern about reporting practices, **1**:157
- education of (1926), **1**:270
- legal liability, **1**:248-259
- legal responsibility, course in, **2**:294
- standard form of report, **1**:178-179

Accountant, The, **1**:21, **1**:46, **1**:49
Accountants' Index, **1**:138, **1**:305, **1**:306, **2**:358
Accountants' Legal Responsibilities (Levy), **1**:249
Accounting
- American beginnings, **1**:6-7
- beginnings, **1**:13-22
- business and tax, **2**:400-403
- centralized system, for federal government, **2**:419
- common-law approach, **2**:70
- curriculums, **1**:265-267
- education, *see* Education
- emergence of professional standards, **1**:74-94
- "entity theory," **1**:16
- future, **1**:8-9
- government, *see* Government accounting manpower, during World War II, **2**:46-48
- opportunities for service, **1**:12
- past, **1**:5-7
- personnel, **1**:151-154
- practitioners, challenges to, **2**:8-12
- present, **1**:1-3
- price-level, **2**:68-70
- problems confronted, **1**:7-8
- professional organizations, beginnings, **1**:19-21
- SEC authority to prescribe rules, **1**:191-192, **1**:193
- services, classification of, **1**:266
- standards, lack of, **1**:47-49
- uniform, *see* Uniform accounting
- women in, **1**:153-154

Accounting aids to developing countries, statement on, **2**:371-372
"Accounting and Auditing Approaches to Inventories," **2**:371
Accounting Careers Council, **2**:307
"Accounting Concepts and Standards Underlying Corporate Financial Statements," **2**:71

Accounting court, proposal for, **2**:124-127
Accounting Evolution to 1900 (Littleton), **1**:13n, **1**:306
Accounting firms
attitude of large firms, **2**:368
bankers' influence on switch to large firms, **2**:353-355
consultation with large firms, **2**:352-353
future of local firms, **2**:356
mergers, **2**:342-343
small and large, **2**:339-373
"Accounting for Income Taxes," **2**:141
"Accounting for Investors" (Hoxsey), **1**:165
"Accounting for Leases in Financial Statements of Lessors," **2**:141
"Accounting for the Cost of Pension Plans," **2**:141
"Accounting for the Investment Credit," **2**:103
"Accounting Function for Small Business, The" (Witschey), **2**:490
"Accounting Function in Economic Progress, The" (Bevis), **2**:489
"Accounting Has Failed to Prevent Major Misrepresentation," **2**:74-75
"Accounting May Be the Right Field for You," **2**:307
Accounting organizations
reunion, **1**:353-371
schism, **1**:303, **1**:314-352
Accounting practice
description, **1**:10-11
interstate, **1**:286-287
Accounting Practice Management Handbook, **2**:363
Accounting principles
"common-law" approach to, **2**:7, **2**:9
development of, **1**:172-180
Institute stance on, **1**:202-205
"piecemeal" approach, **2**:18
Accounting Principles Board (APB), **2**:90-118, **2**:368, **2**:388, **2**:390, **2**:428, **2**:499.
achievements, **2**:139-142
charter of, **2**:95
increasing authority of, **2**:119-144
Opinions, **2**:95-96, **2**:390
project advisory committee, **2**:97
reorganization, **2**:140
rule on disclosure of departure from Opinions of, **2**:119, **2**:453-454
see also APB Opinions
"Accounting Principles Underlying Corporate Financial Statements," **2**:17
Accounting Profession—Where Is It Headed? The, **2**:492
Accounting research, **2**:91
Accounting Research Bulletin, **2**:79, **2**:82-83, **2**:85-89, **2**:94
No. 1, **2**:7, **2**:14
No. 2, **2**:15
No. 3, **2**:15
No. 32, **2**:66-67
No. 33, **2**:70
No. 44 (revised), **2**:82
Accounting Research Studies, **2**:94
Accounting Review, **1**:262, **1**:263, **2**:70, **2**:194, **2**:197
Accounting Series Releases
No. 1, **2**:8
No. 2, **1**:198, **2**:177
No. 4, **2**:62, **2**:123
No. 21, **2**:148
No. 47, **2**:178
No. 96, **2**:103
No. 102, **2**:131-132
see also Securities and Exchange Commission
Accounting terminology, **1**:76-77, **1**:206
Accounting Terminology, **1**:305
"Accounting — The Language of Business," **2**:306
Accounting Trends and Techniques, **2**:360
Accounts of an Oil Company (Humphreys), **1**:306
Accounts receivable
auditor's responsibility for, **2**:21-22
from officers, employees, or affiliates, **1**:176-177
Accounts—Their Construction and Interpretation (Cole), **1**:102

Adams, Henry C., **1**:75
Adams, Senator, **1**:188
Administration of a tax practice, course in, **2**:293
Administrative practice legislation, **2**:255-257
Administrative Practitioners Bill, **2**:221-222, **2**:227, **2**:229, **2**:237, **2**:239, **2**:242, **2**:250
Adverse opinion, **2**:451
Advertising, **1**:88-93
Committee on professional ethics Opinion No. 11 on, **2**:461-462
first formal rule against, **2**:460
program, **2**:377-378
rules of conduct on, **1**:230-234
"Advisory Accountancy" (Gower), **1**:148
Advisory Commission to the Council on National Defense, **2**:44
Advisory Council of State Society Presidents, **1**:364, **1**:365, **1**:369, **1**:370
Advisory Grading Service, **2**:316
Advisory services, growth of, **1**:146-148
Agency for International Development, **2**:371
Agran, Reuben, CPA v. *Morris Shapiro et al.*, **2**:240, **2**:241, **2**:242, **2**:245, **2**:247, **2**:250
Agriculture Department, **2**:165
American Accountant, The, **1**:312
American Accounting Association, **1**:263, **2**:8, **2**:11, **2**:16, **2**:17, **2**:59, **2**:64, **2**:70, **2**:76, **2**:96, **2**:107, **2**:118, **2**:124, **2**:192, **2**:260, **2**:261, **2**:262, **2**:263-264, **2**:265, **2**:268, **2**:279, **2**:284, **2**:285, **2**:303, **2**:307, **2**:314, **2**:318, **2**:416
American Association of Collegiate Schools of Business, **2**:260, **2**:261, **2**:268, **2**:277, **2**:284, **2**:314
American Association of Public Accountants, **1**:6, **1**:22-23, **1**:30, **1**:31, **1**:38, **1**:45, **1**:47, **1**:53, **1**:57, **1**:59, **1**:63, **1**:65, **1**:69, **1**:228, **1**:260, **1**:317, **2**:1
American Association of University Instructors in Accounting, **1**:261, **1**:262
American Bankers Association, **1**:241, **2**:134, **2**:168-169, **2**:200, **2**:355, **2**:399
Credit Policy Committee, **2**:381
American Bar Association, **1**:220, **2**:205, **2**:326, **2**:362, **2**:399, **2**:405, **2**:413, **2**:478-479
Canons of Ethics, **2**:449
disagreement over tax practice, **1**:224-227, **2**:206-257
House of Delegates, **2**:218, **2**:219, **2**:225, **2**:227, **2**:248, **2**:249, **2**:250, **2**:252
Special Committee on Unauthorized Practice of the Law, **1**:225, **1**:226, **2**:206
American Economic Association, **1**:82, **1**:250
American Institute Benevolent Fund, Inc., **1**:307
American Institute of Accountants, **1**:194, **1**:220, **1**:260, **1**:298, **1**:308, **1**:310, **2**:1, **2**:43, **2**:52, **2**:74, **2**:327, **2**:343, **2**:408, **2**:469
CPA vs., **1**:318-320
educational activities, **1**:263
SEC and, **1**:194-196
state societies vs., **1**:320-321
see also Institute of Accountants in the United States of America, formation of
American Institute of Certified Public Accountants, **1**:3, **1**:6, **1**:361, **2**:58, **2**:59, **2**:138, **2**:171, **2**:173, **2**:203, **2**:284, **2**:307, **2**:314, **2**:344, **2**:434-438
action in Washington, **2**:362
advisory committee of local practitioners, **2**:350-351
attitude of large firms, **2**:368
computer program, **2**:364-365
continuing education, **2**:361
disagreement with Bar Association, **2**:206-257
evaluation of audit capacity, **2**:366-368
insurance plans, **2**:361-362
international affairs, **2**:369-372
library and information service, **2**:358
management services, **2**:363-364
membership relations, **2**:349-350

membership services, **2**:357
objectives, **2**:501-503
practice management, **2**:363
publications, **2**:359-360
public relations activities, **2**:350-351
state society relations, **2**:345-349
Washington office, **2**:435-439
see also American Institute of Accountants
see also Institute of Accountants in the United States of America, formation of
American Institute of Consulting Engineers, **2**:35
American Institute of Public Accountants—Its First Twenty Years (Webster), **1**:25n
American Institute Publishing Company, **1**:306
American Management Association, **1**:151, **1**:168, **1**:200, **2**:295
American Medical Association, **2**:362
American Municipal Association, **2**:416
American Petroleum Institute, Committee on Uniform Methods of Oil Accounting, **1**:211
American Society of Certified Public Accountants, **1**:330-371 *passim*, **2**:1, **2**:416
American Society of Women Accountants, **2**:307
American Tobacco Company, **1**:71, **1**:83
American Trade Association Executives, **1**:151
American Woman's Society of Certified Public Accountants, **1**:153
Amicus curiae, Institute as, **1**:254
Analysts, pressure for comparability, **2**:71-72
Andersen, Arthur, **1**:158
Andersen, Arthur & Co., **1**:154, **2**:131
Andrews, Frederick B., **1**:174, **1**:236
Andrews, T. Coleman, **2**:69, **2**:383, **2**:405, **2**:416, **2**:424, **2**:427
Ankers, Raymond G., **2**:291
Annual reports, Institute, **2**:380-381
Anti-trust laws, and rule on competitive bidding, **2**:466-468
Anyon, James T., **1**:26, **1**:33, **1**:37, **1**:38, **1**:49, **1**:251
Recollections of the Early Days of American Accountancy 1883-1893, **1**:26n
APB Opinions
No. 2, **2**:100-103, **2**:106, **2**:115
No. 3, **2**:139
No. 4, **2**:103-104, **2**:133
No. 5, **2**:140
No. 6, **2**:141
No. 7, **2**:141
No. 8, **2**:141
No. 9, **2**:134, **2**:141
No. 10, **2**:138, **2**:141
No. 11, **2**:134, **3**:138, **2**:141
No. 12, **1**:142
No. 13, **2**:134, **2**:142
No. 14, **2**:134, **2**:142
"Approved Methods for the Preparation of Balance Sheet Statements," **1**:133, **2**:20, **2**:146
Arbitration Society of America, **1**:298
Armistead, George, **1**:358, **1**:360, **1**:367
Associate Chartered Accountant, **1**:20
Association of CPA Examiners, **1**:275, **2**:265, **2**:284, **2**:316, **2**:319, **2**:445
Association of Governing Boards of State Universities and Allied Institutions, **1**:332
Association of the Bar of the City of New York, **2**:244
Atlantic Monthly, **1**:162
Attestation of tax returns, **1**:215-216
Audit capacity, evaluation of, **2**:366-368
Audit certificate, 1929 form, **1**:160
Audit companies, **1**:87, **1**:244-245, **2**:468-469
Audited financial statements, first, **1**:6
Audit guides, **2**:150
Auditing
crisis in, **2**:20-41
procedural guidelines, **2**:149-150

voluntary quality control in, 2:368
Auditing (Montgomery), 1:101, 1:253
Auditing: A Practical Manual for Auditors (Dicksee), 1:101, 1:102, 1:249
Auditing and EDP, 2:164, 2:365
Auditing procedure, extensions of, 2:33-35
Auditing standards and procedures
  banks' influence in enforcing, 2:168-169
  categories of, 2:148-149
  codification of, 2:162-164
  compliance with, 2:164-165
  concept of, 2:147-149
  courts' influence in, 2:170-173
  disciplinary machinery, 2:165-168
  SEC influence on, 2:155-158
"Auditing Standards and Procedures," 2:163
Auditor (s)
  certificates, reports, opinions, 2:151-158
  exceptions and disclaimers, 2:159-162
  increasing visibility of, 1:144-146
  responsibility for inventories and receivables, 2:21-22
  see also McKesson & Robbins case
Auditor, The, 1:52
"Auditor's Approach to Statistical Sampling, An," 2:164
Auditor's certificate (1903), 1:28-29
"Auditors Have Arrived, The" (Wise), 2:386-389
"Auditor's Opinion on the Basis of a Restricted Examination, The," 2:38
Auditor's report, evolution of, 2:151-155
"Auditor's Report: Its Meaning and Significance, The," 2:169
Audit responsibility, 2:145-178
Audits
  savings and loan, 1:211
  year-end, 1:149-151
"Audits by Certified Public Accountants" ("Red Book"), 2:163
"Audits of Banks," 2:164
"Audits of Brokers or Dealers in Securities," 2:164
"Audits of Construction Contractors," 2:164
"Audits of Corporate Accounts," 1:175-179, 1:182, 2:5, 2:20
"Audits of Fire and Casualty Insurance Companies," 2:164
"Audits of Savings and Loan Associations," 2:164
"Audits of Voluntary Health and Welfare Organizations," 2:164
Audit Working Papers (Jackson), 1:305
Auerbach Corporation, 2:365
Austin, Maurice, 2:414n
Axelson, Kenneth, 2:498

Bache & Co., 1:251
Badillo, Herman, 2:383
Bailey, George D., 2:65-66, 2:68, 2:69, 2:269, 2:288
Bailey committee, 2:269, 2:272
  report, 2:269-271
Baker, John A., Jr., 2:320n
Balance sheet, in registration statement, 1:190
Balance-Sheet, The (Couchman), 1:171, 1:305
Bankers
  influence on switch to large firms, 2:353-355
  relations with, 1:291-296
  support for independent audit, 1:293
Banking Law Journal, 1:48
Banks, influence in enforcing auditing standards and procedures, 2:168-169
Barkley, Senator, 1:185-190 *passim*
Barnard, Chester I., 2:69
Barnes, William T., 2:414n
Barr, Andrew, 2:92, 2:110, 2:133, 2:184-185
Barron's, 2:105, 2:389
Barrow, John Wylie, 1:36
Barrow, Wade, Guthrie & Co., 1:26, 1:27, 1:36, 1:171, 1:175, 1:251, 2:29

Bartelt, E. F., 2:417, 2:418, 2:420, 2:428
"Basic Postulates of Accounting, The" (Moonitz), 2:97
Basic Standard Costs (Camman), 1:306
Beame, Abraham, 2:383
Beamer, Elmer G., 2:276, 2:281
Beamer committee, 2:281-282, 2:286
recommendations, 2:283-284, 2:315
Bedford, Norton M., 2:490
"Education for Accounting as a Learned Profession," 2:491
Benevolent fund, 1:307
Bennett, George E., 1:267
Fraud, Its Control Through Accounts, 1:305
Bercu, 2:219-221, 2:224, 2:225, 2:234, 2:235, 2:236, 2:240
Bercu, Bernard, 2:219-220
Berg, Ernest A., 2:320n
Berger, Robert O., 1:358
Berle, Adolf A., Jr., 1:170, 1:173-174, 1:182, 1:191
Modern Corporation and Private Property, The (with G. C. Means), 1:170, 1:173
"Public Interest in Accountancy," 1:172-173
Beta Alpha Psi, 1:270-271
Bevis, Herman W., 2:320n, 2:486, 2.489, 2:490, 2:491
"Accounting Function in Economic Progress, The," 2:489
"CPA's Attest Function in Modern Society, The," 2:491
Bidding, 1:87-88
Biltmore Hotel, 2:297
Blake, Matthew F., 2:481
Blakley, William A., 2:383
"block time," on data-processing equipment, 2:471
Blough, Carman G., 1:199, 1:201, 2:8, 2:9-12, 2:13, 2:17, 2:49, 2:69, 2:85, 2:87-88, 2:91-92, 2:99, 2:104, 2:118, 2:156-157, 2:288
Board of Examiners, 1:264, 1:272, 1:273, 1:274, 1:319, 1:334, 1:335, 1:337, 1:343, 1:345, 2:264, 2:291, 2:316-317, 2:318, 2:487
Board of Tax Appeals, 1:222-227, 1:342, 1:344, 2:205, 2:207, 2:209, 2:214
"boiler plate," 2:461
Boodell, Tom, 2:245, 2:246
Bookkeeping, double-entry, beginnings, 1:14
Bordner, Howard W., 2:425
Boucher, Charles A., 2:384
Bowman, Archibald, 1:175
Bows, Albert J., 2:118
Briggs, Robert T., 2:69
Briloff, Abraham J., 2:197-198, 2:199
"Old Myths and New Realities in Accountancy," 2:197
Brink, Victor Z., 2:50
British Companies Act, 1:182
Broad, Samuel J., 1:205, 2:33, 2:38, 2:52-53, 2:66, 2:69, 2:150, 2:181, 2:288
Brokers' accounts, 1:158
Brookings Institution, 2:356, 2:419-420, 2:423
report on the federal financial system, 2:419
Browne, Dudley E., 2:92
Brundage, Percival F., 2:68, 2:69, 2:227, 2:230, 2:236-237, 2:238, 2:263, 2:288, 2:383
Bruschi, William C., 2:281, 2:320n
Bryan, Lyman, 2:436
Buchan, Leslie J., 2:265
Budget, federal, 1:296-297
Budget and Accounting Act of 1921, 1:296, 2:416, 2:429
Budget and Accounting Procedures Act of 1950, 2:427, 2:429, 2:433
"Building and Accounting Practice," 2:297
Bureau of Internal Revenue, 1:150, 1:151, 1:213, 1:218, 1:221, 2:49, 2:204, 2:225, 2:228, 2:237, 2:396, 2:397, 2:399
Income-Tax Unit, Special Assignment Section, 1:214
reorganization of, 2:405-406
Special Committee on Appeals and Review, 1:222, 1:223
see also Board of Tax Appeals; Internal Revenue Service

Bureau of Placements, **1**:276-278, **2**:300
Bureau of public affairs, **1**:298, **1**:300
Bureau of the Budget, **1**:296, **2**:416, **2**:420, **2**:421, **2**:422, **2**:423, **2**:431
Burns, Donald T., **2**:414n
Burrows, H. W., **2**:45
Business, **1**:48
Business accounting, tax accounting and, **2**:400-403
"Business Combinations," **2**:89
Business Week, **2**:25, **2**:104, **2**:389
Business World, **1**:45
Byerly, Francis P., **2**:208, **2**:210, **2**:211, **2**:212
"Relationships Between the Practice of Law and Accounting," **2**:212
Byrd, Harry F., **2**:423, **2**:426

Caffrey, James J., **2**:86
Caffyn, Harold R., **2**:302-303
California Society of Certified Public Accountants, **2**:289, **2**:293, **2**:466, **2**:490
California State Bar, **2**:250
Camman, Eric, **2**:288
Basic Standard Costs, **1**:306
Campbell, Joseph, **2**:383, **2**:431
Campbell, William B., **1**:157
Campbell v. *McIntyre,* **1**:285
Canadian Institute of Chartered Accountants, **2**:306, **2**:371
"Canned newsletters," **2**:460-461
Cannon, Arthur M., **2**:92
Cannon, James G., "The Relationship of the Banker to the Public Accountant," **1**:103
Capital surplus, **1**:176
Caplin, Mortimer M., **2**:481
Cardozo, Benjamin, **1**:256-258
Carey, John L., **1**:348, **2**:500
Carlson, Frank, **2**:399
Carlson Bill, **2**:400
Carnegie Foundation, **2**:494
report, **2**:273-276, **2**:280
Carter, Arthur H., **1**:175, **1**:184, **1**:355, **2**:45
testimony before Senate Committee on Banking and Currency, **1**:185-190
Cary, William L., **2**:106, **2**:107, **2**:109-110
"Cash-flow Analysis and the Funds Statement" (Mason), **2**:97
Cemetery Accounts (Mucklow), **1**:306
Century Company, **1**:206, **1**:305, **1**:348
Certificates
auditors', **1**:151-158
qualified, **1**:82-83
Certified Public Accountant, The, **1**:331, **2**:50, **2**:359
Chamberlain, Richard S., **2**:484n
Chamber of Commerce of the United States, **1**:223
Champion, John, **2**:384
Chapman, Richard M., **1**:44
Charles, William, **2**:216
Chase, Harvey S., **1**:63, **1**:125, **1**:131, **1**:296, **2**:415
Cincinnati School of Commerce and Accounts, **1**:97
Circular of Information, **1**:264
City College of New York, Baruch School of Business and Public Administration, **2**:197
Civil Aeronautics Board, **2**:125, **2**:438
Civil Service Commission, **1**:216
Clader, Will-A., **1**:365, **1**:367
Claims, unjust, **2**:173-174
Claire, Richard S., **2**:14, **2**:16-17, **2**:297
"Classification of Accounting Services," **1**:266, **1**:271
Clayton Antitrust Act, **1**:55
Client, legal liability to, **1**:251
"Clients' Written Representations Regarding Inventories, Liabilities and Other Matters," **2**:38
Cochrane, George, **2**:151-152, **2**:484n
Code of Professional Ethics, **2**:111, **2**:112, **2**:120, **2**:162, **2**:176, **2**:202, **2**:352, **2**:355, **2**:448
Codes of ethics, uniformity among, **2**:445

Cohen, Manuel F., 2:107, 2:131-132, 2:198-199
Cole, William Morse, 1:102
Accounts—Their Construction and Interpretation, 1:102
College of Law and Finance (St. Louis), 1:98
College of Physicians and Surgeons, 2:492
Colley, Frederick G., 1:63
Collins, Clem W., 1:357, 2:13, 2:40
Colorado Midland Railway, 1:30
Columbia Law Review, 2:137
Columbia University
accountancy laboratory, 1:99, 1:170
Bureau of Applied Social Research, 2:308
Council on Research in the Social Sciences, 1:171
Educational Records Bureau, 2:301, 2:302
Commercial and Financial Chronicle, 1:138
Commission on Budget Concepts, 2:433
Commission on Efficiency and Economy, 1:296, 2:415
Commission on Organization of the Executive Branch of the Government, *see* Hoover Commission
Commission on Standards of Education and Experience for CPAs, 2:264-268, 2:275, 2:281
Commission on the Common Body of Knowledge for CPAs, 2:276-277, 2:281
Commissions from the laity, rules of conduct on, 1:245-246
Committee on accounting personnel, 2:292, 2:305
Committee on accounting procedure, 2:12-13, 2:16, 2:28, 2:38, 2:49, 2:63, 2:65, 2:66-67, 2:70, 2:73, 2:77, 2:81, 2:84-89, 2:95, 2:151, 2:450
Committee on auditing procedure, 2:29, 2:33, 2:38, 2:52, 2:118, 2:146, 2:147, 2:149, 2:159, 2:160, 2:163, 2:171, 2:450, 2:451, 2:476
survey on extent of compliance with Statement No. 23, 2:451
see also Statements on auditing procedure
Committee on Business Conduct of the Exchange, 1:158
Committee on co-operation with bankers, 1:238
Committee on co-operation with other organizations, 1:358-367 *passim*
Committee on Co-operation with Public Accountants, 1:295
Committee on co-operation with stock exchanges, 2:5
Committee on co-operation with the Bar Association, 2:205-257 *passim*
Committee on co-operation with the SEC, 2:8
Committee on Department Methods of the United States Government ("Keep Commission"), 1:58
Committee on education, 1:97-100, 1:262, 1:263-270, 2:259-263, 2:288-289
Committee on education and experience requirements for CPAs, 2:281-282
see also Beamer committee
Committee on federal government accounting, 2:428
Committee on federal legislation, 1:131, 1:217, 1:218
Committee on federal taxation, 2:49, 2:395, 2:480, 2:481
subcommittee on responsibilities in tax practice, 2:481
Committee on federal taxation and relations with the Bar, 2:235
Committee on government accounting, 2:416, 2:422-423
Committee on international relations, 2:370-371, 2:372
Committee on inventories: 1:211-212
Committee on long-range objectives, 2:275, 2:334-335, 2:338, 2:486-490, 2:501
successes and defeats, 2:491-492

Committee on management services, 2:202, 2:363, 2:482, 2:483
Committee on personnel reference, 2:291
Committee on placements, 1:270
Committee on professional advancement, 1:297
Committee on professional ethics, 2:118, 2:176, 2:186, 2:187, 2:440-484 *passim*
advertising, question of, 1:230-234
operating problems, 2:446-448
Opinion No. 1, 2:461
Opinion No. 2, 2:462
Opinion No. 6, 2:478
Opinion No. 7, 2:469, 2:470-471
Opinion No. 8, 2:452
Opinion No. 9, 2:461, 2:463, 2:464-465
Opinion No. 10, 2:452
Opinion No. 11, 2:461-462
Opinion No. 12, 2:193-194, 2:457, 2:459, 2:482, 2:483
Opinion No. 13, 2:480
Opinion No. 14, 2:482, 2:483
Opinion No. 15, 2:458
Opinion No. 16, 2:459-460
Opinion No. 17, 2:478, 2:482
Opinion No. 18, 2:468
report on McKesson & Robbins case, 2:38-41
Trial Board, 1:230
Committee on professional relations (American Bar Association), 2:246
Committee on public affairs, 1:298
Committee on relations with public accountants, 2:337
Committee on relations with the federal government, 2:436
Committee on research program, 2:92-94, 2:184
Committee on restrictive legislation, 1:284-285
Committee on savings and loan accounts, 1:211
Committee on selection of personnel, 2:291, 2:302
Committee on state legislation, 1:286, 1:288-289, 2:325-326, 2:331, 2:332-337
Committee on Stock List, *see* New York Stock Exchange
Committee on structure, 2:498, 2:501
Committee on tax accounting practice, 2:479-480
Committee on tax practice, 2:250
Committee on terminology, 1:206
Committee on the problems of federal government accounting, 2:417
Committee on unauthorized practice of the law (American Bar Association), 1:225, 1:226, 2:206-257 *passim*
Common body of knowledge, 2:275-280
"common-law" approach to accounting, 2:7, 2:9, 2:70
Communication, improving, 2:389-391
Comparability, 2:123
countervailing pressure, 2:80-84
industry resistance to, 2:133-135
pressure from academia for, 2:70-71
pressure from accountants for, 2:73-80
pressure from analysts for, 2:71-72
pressure from the press for, 2:72-73
SEC pressure for, 2:130-132
see also Uniformity
"Compatibility of Management Consulting and Auditing" (Schulte), 2:194
Competence, developing standards of, 1:260-278
Competition
in examinations, 1:347-348
intraprofessional, 1:332-336
Competitive bidding, 2:465-468
anti-trust laws and rule on, 2:466-468
rules of conduct on, 1:243-244
Computerized accounting service, rule on incorporation to offer, 2:470-471
Computer Notebook, 2:365
Computer program, 2:364-365

Conduct, *see* Rules of professional conduct . .
Conference on Federal Government Accounting, **2**:420-421, **2**:430
Conference on Municipal Accounting, **2**:417-420
Confidential relationship, rule on, **2**:475-476
Conflict of interest, appearance of, **2**:193-194, **2**:457
see also Independence
"Congress and the Tax Lobbyist—How Special Tax Provisions Get Enacted" (Surrey), **2**:411-412
Congressional Joint Committee on Reduction of Non-essential Federal Expenditures, **2**:422, **2**:423
Connecticut Society of Certified Public Accountants, **2**:465
"Consolidated Financial Statements," **2**:89
"Constructive fraud," **1**:258
Consulting activities during World War II, **2**:48-49
Contemporary Accounting, **2**:287-288, **2**:289
Contingent fees
disclosure of, **1**:236
rules of conduct on, **1**:234-237, **2**:476
"Contingent Liability under Policies with Mutual Insurance Companies," **2**:38
Continuing education, **2**:361
program of, **2**:291-294
recruiting and, **2**:286-310
Controller, The, **1**:313
Controllers Institute of America, **1**:178, **1**:312-313, **2**:35, **2**:59, **2**:62, **2**:74, **2**:81, **2**:92
Conway, **2**:223-242 *passim*
Cook, Donald, **2**:384
Cooper, John Alexander, **1**:91
"Should Accountants Advertise?" (with Gore and Shorrock), **1**:91-92
Cooper, Walter A., **2**:414n
"Co-operation Between Lawyers and Accountants in Tax Practice" (Otterbourg), **2**:235
Corporate Profits as Shown by Audit Reports (Paton), **1**:301
Corporation
beginnings, **1**:16-17
excise tax, **1**:64-67
Corporation Excise Tax Law of 1909, **1**:64, **1**:213
impact on accounting, **1**:67-68
Corporation Tax Law, **1**:292
Correa, Mathias F., **2**:220, **2**:235, **2**:240
Couchman, Charles B., **1**:171-172, **1**:175, **1**:350, **1**:357-358
The Balance Sheet, **1**:171, **1**:305
Council of National Defense, **1**:141
Courses, Institute, **2**:291-294
accountants' legal responsibility, **2**:294
administration of a tax practice, **2**:293
report writing, **2**:293
Courts, influence on auditing standards and procedures, **2**:170-173
Covington, J. Harry, **1**:183, **1**:184, **1**:282
Covington & Burling, **2**:235
CPA (s)
advisory role, **1**:9
association, pressure for formation of, **1**:111-113
audio program, **2**:299
examination, *see* Uniform CPA Examination
Institute vs., **1**:318-320
requirements, legal regulation and, **2**:311-338
social responsibility, **1**:2
standards, education and, **1**:95-107
"CPA, The" **2**:306
"CPA Audits and Gobbledygook Guides," **2**:137
CPA certificate
educational requirements, **2**:312-313
experience requirements, **2**:314-315
legal requirements, **2**:311-312
uniform examination for, **1**:105
CPA examination, **2**:315-320

accounting curricula and, **2**:319-320
grading procedures, **2**:318
tests of validity, **2**:319
uniform, **2**:315
CPA Handbook, The, **2**:290-291
CPA law, first, **1**:43-45
CPA Laws of the United States, **1**:305
CPA movement, **1**:102-107
CPA Plans for the Future, The, **2**:494, **2**:495-496
"CPA's Attest Function in Modern Society, The" (Bevis), **2**:491
"CPA Under Fire," **2**:136
Craig v. *Anyon,* **1**:251
"Credit Frauds," **1**:300
Credit men, support for independent audits, **1**:293
"Crime Tendency, The," **1**:298
Cromwell, Seymour L., **1**:160, **1**:161

Dartmouth College, Amos Tuck School, **1**:97, **1**:98
Data processing service, **2**:469-471
Davies, W. Sanders, **1**:46, **1**:119, **1**:121, **1**:125, **1**:136, **1**:141, **1**:320, **1**:322
Davis, Gordon, **2**:365
Dean, Arthur H., **2**:69
"Declining-balance Depreciation," **2**:82
revised, **2**:89
Deferred tax account, **2**:82
Del Sesto, Christopher, **2**:383
Denit, J. Darlington, **2**:420
Department of Agriculture, **2**:421, **2**:423
Department of Commerce, **1**:173
Department of Defense, **2**:430, **2**:438
Department of Health, Education and Welfare, **2**:438, **2**:458-459
Depression, Great, **1**:154-155
"Description of the Professional Practice of Accounting by Certified Public Accountants," **2**:497, **2**:503
"Description of the Professional Practice of Certified Public Accountants," **1**:10, **2**:283
Detroit Economic Club, **2**:381
Developing countries, statement on accounting aids to, **2**:371-372
deVerges, **1**:282
Devore, Malcolm M., **2**:199, **2**:200, **2**:202, **2**:491
Diamond, Samuel I., Jr., **2**:320n
Dickinson, Arthur Lowes, **1**:28, **1**:51, **1**:57, **1**:75, **1**:79, **1**:136
Dicksee, Lawrence R., *Auditing: A Practical Manual for Auditors,* **1**:101, **1**:102, **1**:249
Dingell, Representative, **2**:213, **2**:214
"diploma mill," **1**:281
Disciplinary machinery, **2**:165-168
Disciplinary proceedings, co-ordination of, **2**:444-446
Disclaimers, exceptions and, **2**:159-162
Disclosure, **1**:83-84
contingent fees, **1**:236
forecasts, **2**:452
material departure from generally accepted accounting principles, **2**:454-455
pressure for, **1**:57-58
sales, **1**:196-197
"Disclosure of Supplemental Financial Information by Diversified Companies," **2**:142
Dividend on treasury stock, **1**:176
Doherty, William, **2**:359
Dohr, James L., **1**:261, **2**:16, **2**:69, **2**:290
Dominion Association of Chartered Accountants of Canada, **2**:303
Double-entry bookkeeping, beginnings of, **1**:14
Dun & Bradstreet, **1**:151, **1**:294
Dupont Powder Company, **1**:71
Duties of the Junior Accountant, The (Reynolds and Thornton), **1**:138, **1**:305
Duties of the Senior Accountant (Thornton), **1**:306

Earned surplus, **1**:158-159, **1**:176
defined, **1**:158
Earnings, pressure for comparability of, **2**:56-89
Earnings per share, focus on, **2**:58-60
East India Company, **1**:16
Eaton, Marquis G., **2**:77-80, **2**:160, **2**:288, **2**:289-290, **2**:294-295, **2**:296, **2**:352, **2**:353, **2**:363, **2**:479, **2**:485-486
Education
"catch-up," **2**:286
continuing, *see* Continuing education
CPA standards and, **1**:95-107
efforts to improve, **1**:96-100
experience and, **2**:258-285
requirements for CPA certificate, **2**:312-313
Educational activities, **1**:263
Educational policies, **1**:267-270
Educational requirements for CPA certificate, **2**:312-313
Educational standards, proposed, **2**:259-264
"Education for Accounting as a Learned Profession" (Bedford), **2**:491
Eisenhower, Dwight D., **2**:431
Elijah Watt Sells medal
see Sells medal
Ellis, George P., **2**:414n, **2**:416, **2**:420, **2**:421, **2**:424
Elwell, Fayette H., **1**:260
Employment offers, rule of conduct on, **1**:234
Employment of lawyers, **2**:478-479
Endowment fund, **1**:304, **1**:305
English Companies Act, **1**:75, **1**:161, **1**:163, **1**:294, **2**:5
Equitable Life Assurance Society, **1**:29, **1**:57
Ernst, A. C., **1**:233-234
Ernst & Ernst, **1**:233-234
Eskew, Samuel W., **2**:484n
"Establishing Accounting Principles —A Crisis in Decision-Making," **2**:124
Estes, Billie Sol, **2**:165-166
Ethical responsibilities, **2**:440-484
Ethical Standards of the Accounting Profession, **2**:448
Ethics
as examination subject, **2**:446
problems of, **1**:218-219
self-discipline and, **1**:228-247
see also Committee on professional ethics; Rules of professional conduct
Ethics committee, *see* Committee on professional ethics
"Ethics of Accountancy, The" (Joplin), **1**:90
Ethics of a Profession (Richardson), **1**:305
Evening School of Accounts and Finance, **1**:51
"Examination of Financial Statements by Independent Public Accountants," **2**:21, **2**:24, **2**:27, **2**:150, **2**:163
Examinations, competition in, **1**:347-348
Exceptions, disclaimers and, **2**:159-162
Excess-profits-tax Review Board, **1**:142
Excise tax, corporation, **1**:64-67
"Expanding World of Accounting, The," **2**:380
Experience
education and, **2**:258-285
requirements for CPA certificate, **2**:314-315
Export Control Board, **2**:44
"Extensions of Auditing Procedure," **2**:35, **2**:37, **2**:38, **2**:41, **2**:146, **2**:158, **2**:159, **2**:451

Fabricant, Solomon, **2**:69
Farm Credit Administration, **2**:426, **2**:437
Farrand, George M., **2**:17, **2**:50
Federal Accountant, The, **2**:434
Federal budget, **1**:296-297
Federal Communications Commission, **2**:125
"Federal Control of Corporations" (Montgomery), **1**:72

Federal financial system, Brookings Institution report on, **2**:419
Federal government
appeals to, in tax practice dispute, **2**:225-226
impact on accounting, **1**:53-73
Federal Government Accountants Association, **2**:307, **2**:433-434
Federal government corporations, **2**:422-426
Federal Home Loan Bank Board, **1**:211, **2**:437
Federal Power Commission, **2**:69, **2**:125, **2**:438
Federal Public Housing Authority, **2**:426
Federal recognition, question of, **1**:321-322
Federal Reserve Act of 1913, **1**:56, **1**:62
Federal Reserve Board, **1**:56, **1**:62, **1**:63, **1**:118, **1**:129-134 *passim*, **1**:203, **1**:205, **1**:280, **1**:293, **2**:20, **2**:146
Federal Reserve Bulletin of 1917, **1**:132-135, **1**:144, **1**:145, **1**:178, **2**:20, **2**:26, **2**:33, **2**:38, **2**:146, **2**:152, **2**:163
1929 revision, **1**:159-160, **2**:20
1936 revision, **1**:205, **2**:20-21
"Federal Tax Simplification," **1**:300
Federal Trade Commission, **1**:55, **1**:62-63, **1**:129-134 *passim*, **1**:162, **1**:180, **1**:182, **1**:186, **1**:192, **1**:195, **1**:203, **1**:242, **1**:355, **2**:146
Federation of Societies of Public Accountants in the United States of America, **1**:40, **1**:49-51 *passim*, **1**:124
Fellow Chartered Accountant, **1**:20
Fertig, Paul, **2**:293
"Fifty-three Jurisdictions" (Heimbucher), **2**:344, **2**:491
Fifty Years of Accountancy (Montgomery), **1**:30
Financial Analysts Federation, **2**:72, **2**:131, **2**:143, **2**:200
Financial Analysts of Philadelphia, **2**:74
Financial Examinations (Thornton), **1**:306
Financial Executives Institute, **1**:313, **2**:59, **2**:106, **2**:133, **2**:143, **2**:200, **2**:307
"Financial Health of Small Business, The," **2**:381
Financial management, in government functions, **2**:427
Financial Record, The, **1**:48
Financial reporting
drive for better, **1**:156-180, **2**:1-19
public spotlight on, **2**:384-386
rationale for, **2**:6
"Financial Reporting in a Changing Society," **2**:78-79
Financial reporting practices, accountants' concern about, **1**:157
"Financial Statement Provisions in Term-Loan Agreements," **2**:169
Financial statements
beginnings, **1**:15-16
independently audited, **1**:129-132
pro forma, **1**:295
Financial system, federal, Brookings Institution report on, **2**:419
Finney, H. A., *Introduction to Actuarial Science,* **1**:305
First Fifty Years, The, **1**:154
First National City Bank, **2**:129
Flynn, Thomas D., **2**:121, **2**:125-126, **2**:254, **2**:256, **2**:291, **2**:484n
Folsom, Marion, **2**:241, **2**:242, **2**:251
Forbes, **2**:105, **2**:136, **2**:138, **2**:389
Forbes, John F., **1**:93, **1**:119, **1**:120, **1**:121, **1**:172, **1**:204, **1**:272, **1**:318, **1**:325, **1**:326, **1**:335, **1**:349, **1**:350, **1**:351-352, **1**:354-355, **1**:359
Ford, Gordon, **2**:496
Ford Foundation report, **2**:273-276, **2**:280
Forecasts, full disclosure on, **2**:452
Fortune, **1**:168, **2**:105, **2**:341, **2**:386
Foye, Arthur B., **2**:240-243 *passim*, **2**:250, **2**:290
Francis, John W., **1**:51
Frank, Jerome N., **2**:63
Franke, William B., **1**:206, **2**:383
Fraud, Its Control Through Accounts (Bennett), **1**:305
Freeman, Orville, **2**:166-167

Frese, Walter F., **2**:428
"Frustrated CPAs—Accounting Body Fails in Attempts to Change Some Firms' Reporting," **2**:138
Full disclosure on forecasts, **2**:452

Gardner, John W., **2**:276, **2**:494
General Accounting Office, **1**:296, **2**:48, **2**:416, **2**:418, **2**:420, **2**:421, **2**:422, **2**:423, **2**:432
  Corporate Audits Division, **2**:425, **2**:426
General Electric Company, **1**:165, **2**:487
Generally accepted accounting principles, **2**:78-79
  disclosure of material departure from, **2**:454-455
  press criticism of, **2**:135-139
  validity of term, **2**:111
"Generally Accepted Auditing Standards—Their Significance and Scope," **2**:148-149
General Munitions Board, **1**:141
"General Recognition of Accountancy as a Profession," **2**:380
Gerfen, Richard, **2**:289
G.I. Bill of Rights, **2**:57
Giffen, Hilliard R., **2**:445
Gilman, Stephen, **2**:69
Glover, Patrick W. R., **2**:29, **2**:33
Goodloe, J. S. M., **1**:334
Gordon-Howell report, **2**:273-276
Gore, Edward E., **1**:91-92, **1**:215-216, **1**:223-224, **1**:334, **1**:335, **1**:337, **1**:338, **1**:342, **1**:345, **1**:346
  "Should Accountants Advertise?" (with Cooper and Shorrock), **1**:91-92
Gore, Senator, **1**:186-190 *passim*
Gottsberger bill, **1**:43
Government accounting, **1**:58-59
  improving, **2**:415-439
  local, **2**:438-439
Government Corporation Control Act (Public Law 248), **2**:423, **2**:424
Gower, William B., "Advisory Accountancy," **1**:148
Graber, Paul L., **2**:85
Graduate-study conferences, **2**:263, **2**:289
Grady, Paul, **2**:45, **2**:92, **2**:118, **2**:140, **2**:150, **2**:430
  "Inventory of Generally Accepted Accounting Principles for Business Enterprises," **2**:142
  Memoirs and Accounting Thought of George O. May, **1**:132n
Graves, Thomas J., **2**:414n
Greeley, Harold Dudley, *Law for Laymen*, **1**:306
Green, Thomas J., **2**:414n
Greendlinger, Leo, **1**:101
Greenleaf, Robert, **2**:498
Greer, Howard C., **1**:261, **1**:262, **2**:69
Griswold, Erwin, **2**:243-245, **2**:254
Grosse, Richard H., **2**:320n
"Guidelines for Administration of a Management Advisory Service Practice," **2**:364
Guthrie, Edwin, **1**:36-38

Hamel, Charles D., **1**:223, **1**:342, **2**:229
Hansen, George H., **2**:272
Hansen committee report, **2**:272-273
Harlan, Neil, **2**:384
Harrington, Russell, **2**:383
Harrison, Representative, **1**:67
Hartford Times, **2**:25
Harvard Business Review, **2**:389
Harvard Law Review, **2**:411
Harvard University Graduate School of Business Administration, **1**:98, **1**:104
Haskins, Charles Waldo, **1**:30
Haskins & Sells, **1**:29, **1**:30, **1**:93
  Foundation, **2**:13
Hastings, James J., **1**:358
Hatfield, Henry Rand, **1**:102, **1**:261, **2**:13
  Modern Accounting, **1**:102
  "Statement of Accounting Principles, A" (with Sanders and Moore), **2**:13
Hayden, Stone Incorporated accounting forum, **2**:122

Headquarters offices, Institute, 1:304
Heimbucher, Clifford V., 2:112-113, 2:117, 2:119, 2:120-121, 2:140, 2:276, 2:370, 2:490, 2:491, 2:495
"Fifty-three Jurisdictions," 2:344, 2:491
Heins, John, 1:31, 1:37, 1:38
"Helping the Taxpayer," 2:243, 2:306
"Helping the Taxpayer—A Discussion of Current Issues Affecting Professional Services in the Field of Federal Taxes," 2:243
Hepworth, Samuel R., 2:265
Hewitt, George A., 2:484n
Higgins, Thomas G., 1:154, 2:12, 2:187-188, 2:484n
Hilton, W. P., 1:327
Himmelblau, David, 1:262
History of the Institute of Chartered Accountants in England and Wales (Howitt), 1:20n
Hoenemeyer, Frank, 2:200
Holm, William H., 2:320n
Home Owners Loan Corporation, 2:426
Hoover, Herbert, 2:428
Hoover Commission, 2:426, 2:431, 2:435
Budget and Accounting Task Force, 2:430
proposals, 2:428-431
Task Force on Lending Agencies, 2:430
Hope, J. William, 2:320n
Horizons for a Profession (Roy and others), 2:277-286 *passim,* 2:314
Hosmer, W. Arnold, 2:14
House Committee on Interstate Commerce, 1:184
House Judiciary Committee, 2:222, 2:256
House of Representatives Committee on Interstate and Foreign Commerce, 2:108-110
House organs, rule on distribution of, 2:461
House Ways and Means Committee, 1:223, 2:213, 2:228, 2:242, 2:399, 2:400, 2:402, 2:403
Housing and Home Finance Agency, 2:437
"How Can CPAs Meet Present-Day Challenges of Financial Reporting?" 2:90-92
Howitt, Sir Harold, *History of the Institute of Chartered Accountants in England and Wales,* 1:20n
Hoxsey, J. M. B., 1:164, 1:165, 1:166, 1:182
"Accounting for Investors," 1:165
Hughes, Charles Evans, 1:29
Hull, Cordell, 1:70
Humphrey, George, 2:241
Humphreys, H. G., *The Accounts of an Oil Company,* 1:306
Hunter, Joel, 1:291, 1:292
"The Public Accountant and the Credit Man," 1:291
Hurdman, Frederick H., 1:240, 1:242, 1:309, 1:349, 1:350, 1:358, 1:360-364, 1:367-369, 2:484n
Hurdman & Cranstoun, 1:240
Hurley, Edwin N., 1:63, 1:129-133 *passim,* 1:216
Hutchinson, William P., 2:337

Illinois Society of Public Accountants, 1:49, 1:195, 2:78, 2:183
"Inc.," 2:306
Income statement, all-inclusive vs. earning-capacity, 2:65-67
Income-Tax Law (1913), 1:67-71
Incompatible occupations, rules of conduct on, 1:246
Incorporation
modification of rule on, 2:473
resolution on, 2:473-474
rule on, 2:470-471
Independence, 1:88, 1:197-198
appearance of, 2:176-178
concept of, 2:175-203
financial interest in audit client, 2:456-457
in fact, 2:179-180
in the Medicare environment, 2:458-459

management services and, **2**:191-199
rule on impairment when retired partner is client stockholder or director, **2**:459-460
rule on service as director of non-profit organization, **2**:458
rules of conduct on, **1**:240-243
SEC rules tightened on, **2**:182-183
"Independence in the Auditor's Mental Attitude and Approach," **2**:179
Independent auditor, financial interest in client, **2**:456-457
"Independent Auditor's Reporting Standards in Three Nations, The," **2**:371
Independent audits
bankers' and credit men's support for, **1**:293
beginnings of, **1**:17-18
standard language for laws on, **2**:437-438
Industrial Revolution, **1**:18
Information bureau, library and, **1**:135-139
Institute of Accountants, **1**:19
Institute of Accountants in the United States of America, formation of, **1**:119-126, **1**:318
Institute of Chartered Accountants, **1**:328
Institute of Chartered Accountants in England and Wales, **1**:20, **1**:37, **1**:77, **1**:115, **1**:126, **1**:300, **1**:314, **1**:318, **2**:151, **2**:263, **2**:371, **2**:373
Institute of Chartered Accountants of Scotland, **1**:19
Institute of Chartered Financial Analysts, **2**:72, **2**:381-382
Institute of Internal Auditors, **2**:307
Insurance plans, **2**:361-362
Inter-American Development Bank, **2**:371
"Internal Control—Elements of a Co-ordinated System and Its Importance to Management and the Independent Public Accountant," **2**:150
Internal Revenue Code, **2**:126, **2**:247, **2**:401, **2**:406
Internal Revenue Department, **1**:67
Internal Revenue Service, **2**:238, **2**:240, **2**:243, **2**:378, **2**:404, **2**:405, **2**:408, **2**:413, **2**:479, **2**:481
see also Bureau of Internal Revenue
Internal split, **1**:359-360
International affairs, **2**:369-372
International Committee for Accounting Co-operation (ICAC), **2**:371
International Congress of Accountants, **1**:30, **1**:49-52, **1**:308-310, **2**:3, **2**:370
International Finance Corporation, **2**:371
International Monetary Fund, **2**:371
International relations, **1**:307-311
Interstate Commerce Act of 1887, **1**:24, **1**:59
Interstate Commerce Commission, **1**:24, **1**:55, **1**:57, **1**:60, **1**:65, **1**:75, **1**:174, **2**:77, **2**:78, **2**:125, **2**:438
Interstate Hosiery Mills, **2**:63
Interstate practice, **1**:286-287
Introduction to Actuarial Science (Finney), **1**:305
Introduction to Corporate Accounting Standards, An, **2**:16
Inventories, **1**:211-212
auditor's responsibility for, **2**:21-22
"Inventories and Receivables of Department Stores, Installment Houses, Chain Stores, and Other Retailers," **2**:38
"Inventory of Generally Accepted Accounting Principles for Business Enterprises" (Grady), **2**:142
Investment Bankers Association of America, **1**:201, **2**:131, **2**:355
Industrial Securities Committee, **1**:295
Investment Company Act of 1940, **2**:60
Investment credit, **2**:98-110

"flow-through" method, **2**:98, **2**:100-101
SEC position on, **2**:105-110
spreading method, **2**:102-103
Investor protection, hearings on, **2**:108-110
Investors, responsibility to, **1**:237-239
Ipswich Mills v. *Dillon*, **1**:254
Ives, Stephen B., **2**:427

Jackson, J. Hugh, **1**:262, **1**:267
Audit Working Papers, **1**:305
Jameson, William J., **2**:246, **2**:249, **2**:250, **2**:251, **2**:254
Jennings, Alvin R., **2**:69, **2**:90, **2**:91, **2**:92, **2**:95, **2**:96, **2**:111, **2**:121, **2**:127, **2**:139, **2**:150, **2**:160, **2**:388
Jensen, Wallace M., **2**:414n
Johns, Ralph S., **2**:484n
Johnson, Charles E., **2**:281, **2**:384
Johnson, Joseph French, **1**:97, **1**:100
Joint Committee on Accounting Education, **2**:313-314
Joint Committee on Internal Revenue Taxation, **2**:396, **2**:400, **2**:403, **2**:404
Joint Financial Management Improvement Program, **2**:426-427, **2**:428, **2**:434, **2**:438
objectives, **2**:431-432
Joint Legislative Committee of the State of New York, **1**:29
Jones, J. Weldon, **2**:420
Jones, Caesar & Co., **1**:27
Joplin, J. Porter, **1**:90-91, **1**:117, **1**:119, **1**:141
"The Ethics of Accountancy," **1**:90
Journal of Accountancy, The, **1**:52, **1**:74, **1**:100, **1**:114, **1**:142, **1**:206, **1**:263, **1**:304-307, **2**:50, **2**:51, **2**:359, **2**:436, **2**:500
1916 survey, **1**:83
"Practitioners Forum," **2**:363
"Tax Clinic," **2**:413
Journal of Commerce, The, **1**:292
Justice Department, **2**:466-468

Kane, Robert L., Jr., **2**:265, **2**:290
Kean, Senator, **1**:189
Keep, Charles H., **1**:58
Keep Commission, **1**:58
Kennedy, Joseph P., **1**:194-195
Kent, Ralph E., **2**:393
Keogh Bill, **2**:362
Kessler, Louis M., **2**:291, **2**:320n
Kester, Roy B., **1**:261, **1**:267, **1**:268, **2**:13, **2**:259, **2**:261
King, Earle, **2**:66, **2**:69, **2**:73, **2**:86, **2**:92
Kingston Cotton Mill, **1**:249
Klein, Joseph J., **2**:39, **2**:484n
Knauth, Oswald W., **2**:77
Knowledge, specialized, *see* Common body of knowledge
Kohler, Eric, **1**:262, **2**:288, **2**:421
Koppenhaver, Robin Dee, **2**:320n
Kracke, Edward A., **2**:148
"Tentative Statement of Auditing Standards—Their Generally Accepted Significance and Scope" (with others), **2**:148
Kreuger, Ivar, ("the match king"), **1**:168
Kreuger and Toll, **1**:168

Land Accounts (Mucklow), **1**:306
Landis, James M., **1**:192, **1**:195, **1**:199
Large firms, *see* Accounting firms
Lasser, J. K., **2**:288
Law and Contemporary Problems, **2**:137
Law for Laymen (Greeley), **1**:306
Lawler, John, **2**:359, **2**:500, **2**:501
Lawrence, Professor, **2**:294
Lawsuits against accounting firms, **2**:472
Lawton, Frederick, **2**:428
Lawyers, employment of, **2**:478-479
"Layman's Guide to Preparing Financial Statements for Churches, The," **2**:381
Legal liability, **1**:248-259
and responsibility, **1**:80-82
to client, **1**:251
to third party, **1**:252

Legal regulation, CPA requirements and, **2**:311-338
Legal requirements for CPA certificate, **2**:311-312
Legal Responsibilities and Rights of Public Accountants (Rich), **1**:306
Legal responsibility, course in, **2**:294
Legislation
  administrative practice, **2**:255-257
  implication of McKesson & Robbins case for, **2**:32
  regulatory, **2**:322-325, **2**:332-333
  restrictive, **1**:282-286
Legislative conferences, **2**:337-338
Legislative problems, **2**:321
Legislative restrictions, **2**:344-345
Leidesdorf, Samuel D., **1**:175
Leland, Thomas W., **2**:287
Levy, Saul, **1**:249, **1**:250
  Accountants' Legal Responsibilities, **1**:249
Liability
  "immeasurable," **1**:194
  insurance, **1**:253-254
  see also legal liability
Library and information bureau, **1**:135-139
Library and Technical Information Service, **2**:358
Licensing restrictions, **2**:344-345
Life Insurance Association of America, **2**:200
Linek, Francis M., **2**:320n
Linowes, David F., **2**:491
Lipscomb, Glenard P., **2**:383
Literature, professional, **1**:100-102
Littleton, A. C., **1**:13, **1**:15, **1**:18, **2**:13
  Accounting Evolution to 1900, **1**:13n, **1**:306
  Introduction to Corporate Accounting Standards, An (with W. A. Paton), **2**:16
Lloyds Underwriters of London, **1**:253
Local firms, *see* Accounting firms
Local government accounting, **2**:438
Loeb, **2**:218, **2**:236
London and General Bank, **1**:249, **2**:152
Long-range objectives
  basic objective, **2**:498-499
  identifying, **2**:486
  members not in practice, **2**:486-488
  relations with other organizations, **2**:488-490
Loomis, John R., **1**:53
Lord, H. M., **1**:296
Los Angeles Municipal Court, **2**:240
Los Angeles Superior Court, **2**:240
Louisiana Purchase Exposition, **1**:49
Ludlam, Charles S., **1**:143
Lybrand, William M., **1**:51, **1**:75
Lybrand, Ross Bros. & Montgomery, **1**:31
Lynn, Edward S., **2**:277, **2**:280
Lytle, Richard C., **2**:140

Macmillan Company, **2**:69
MacNeill, James H., **2**:276, **2**:281
Mahon, James J., **2**:371, **2**:372
Main Street and Wall Street (Ripley), **1**:161
Management audits, **2**:432-433
Management sciences, **2**:55
"Management Service Function in Public Accounting, The" (Trueblood), **2**:491
Management services, **2**:54-55, **2**:341, **2**:363-364
  independence and, **2**:191-199
  responsibilities in, **2**:482-483
Management Services, **2**:360
Marwick, Mitchell & Co., **1**:146, **1**:189
Mason, Perry, **2**:96, **2**:139
Massachusetts Society of Certified Public Accountants, **2**:215
Massachusetts Supreme Court, **2**:215, **2**:218
"match king," Ivar Kreuger, **1**:168
"Matter of Principles Splits CPAs, A," **2**:104
Matthews, George C., **1**:195, **1**:198, **2**:61
Matusiak, Louis W., **2**:296, **2**:298
Mautz, Robert K., **2**:92, **2**:199

Philosophy of Auditing, The, (with H. A. Sharaf), **2**:192
Maxwell, David F., **2**:216-219 *passim,* **2**:222, **2**:230, **2**:233, **2**:234
May, George O., **1**:51, **1**:63, **1**:131, **1**:132, **1**:133, **1**:135, **1**:136, **1**:137, **1**:162-163, **1**:165, **1**:172, **1**:174, **1**:175, **1**:179, **1**:182, **1**:192, **1**:202, **1**:216, **1**:302, **1**:304, **1**:320, **2**:3, **2**:12, **2**:18, **2**:68, **2**:74, **2**:84, **2**:288
  Memoirs and Accounting Thoughts of George O. May (Grady, editor), **1**:132n
McConahey, James E., **1**:267
McCormick, Edward, **2**:384
McDevitt, Edward J., **2**:484n
McEachren, John W., **2**:45
McFarland, Carl, **2**:228, **2**:229
McGinnies Bill, **1**:284
McGladrey, Ira B., **1**:357, **2**:159-160
McGladrey, Hansen & Dunn, **1**:357, **2**:159
McKesson & Robbins case, **2**:22-41, **2**:98, **2**:146, **2**:384
  ethics committee report, **2**:38-41
  hearing before New York Attorney General, **2**:25-29
  implications for legislation, **2**:32
  Institute reaction, **2**:24-25
  SEC findings, **2**:35-38
McKinley, William, **1**:24
McKinsey, J. O., **1**:262
McLaren, Norman L., **2**:43, **2**:46
McLaughlin, Rodney, **1**:37
McLeod, Stuart C., **1**:311-312
Meade, Edward Sherwood, **1**:100
Means, Gardiner C., **1**:170, **1**:182, **1**:191
  The Modern Corporation and Private Property (with A. A. Berle, Jr.), **1**:170, **1**:173
Medicare, **2**:437, **2**:458, **2**:459
Membership services, **2**:357
Members not in practice, status of, **2**:486-488
Memoirs and Accounting Thought of George O. May (Grady), **1**:132n
Mendes, Henry E., **2**:320n
"Men of Account," **2**:306
Mergers, **2**:342-343
Mexican Institute of Certified Public Accountants, **2**:290-291
Michigan Association of Certified Public Accountants, **1**:332, **2**:289, **2**:293
Michigan Board of Accountancy, **1**:332
Middle Atlantic States Accounting Conference, **2**:350
Miller, Philip N., **2**:484n
"Million-Dollar Handbook," **2**:289-291
Mills, Leslie, **2**:45, **2**:414n
Mills, Wilbur D., **2**:228, **2**:229, **2**:407-408
Miltimore, Louise S., **1**:138, **1**:139
Milwaukee Control of Controllers Institute, **2**:77
Minnesota Society of Certified Public Accountants, **2**:223, **2**:230
Minnesota Supreme Court, **2**:233, **2**:234, **2**:242
Mixed partnerships, rule on, **2**:477-478
Modern Accounting (Hatfield), **1**:102
Modern Corporation and Private Property, The (Berle and Means), **1**:170, **1**:173
Montgomery, Robert H., **1**:30, **1**:33, **1**:46, **1**:51, **1**:61, **1**:63, **1**:67, **1**:69, **1**:70, **1**:72, **1**:99, **1**:101, **1**:125, **1**:131, **1**:133, **1**:142, **1**:143, **1**:185, **1**:308-310 *passim,* **1**:323, **1**:341, **1**:354, **1**:358, **1**:365, **1**:367, **2**:398
  as Association president, **1**:115-117
  Auditing, **1**:101, **1**:253
  farewell address, **2**:3-5
  "Federal Control of Corporations," **1**:72
  Fifty Years of Accountancy, **1**:30
Moody's Manual, **1**:138
Moonitz, Maurice, **2**:96
  "Basic Postulates of Accounting, The," **2**:97
  "Tentative Set of Broad Accounting Principles for Business Enterprises, A" (with R. T. Sprouse), **2**:97
Moore, Underhill, "A Statement of

Accounting Principles" (with Sanders and Hatfield), 2:13
Morey, Lloyd, 2:384, 2:416, 2:418, 2:420
Morison, Samuel Eliot, 1:157, 1:182, 2:2
Oxford History of the American People, The, 2:2n
Morris Associates, Robert, 1:145, 1:150, 1:151, 1:157, 1:238, 1:294, 1:295, 2:143, 2:163, 2:168, 2:169
Mucklow, Walter, 1:206
Cemetery Accounts, 1:306
Land Accounts, 1:306
Municipal Finance Officers Association, 2:416
Musica, Philip N., 2:23

NACA Bulletin, 1:312
National Association of Accountants, 2:106, 2:307
National Association of Certified Public Accountants, 1:112, 1:281-282, 1:331, 1:333, 1:337, 1:338, 1:344
"diploma mill," 1:281
National Association of Cost Accountants, 1:147, 1:151, 1:311-312, 2:52, 2:399, 2:416
National Association of Credit Men, 1:151, 1:291, 1:293, 1:300, 2:399
National Association of Manufacturers, 2:59
National Association of State Boards of Accountancy, 1:275, 2:319
National Association of State Insurance Commissions, 1:57
National Bureau of Economic Research, 1:301-302
National Committee on Municipal Accounting, 2:416, 2:417, 2:438-439
National Conference of Bankers and Certified Public Accountants, 2:168
National Conference of Lawyers and Certified Public Accountants, 2:216-257 *passim,* 2:326, 2:479
statement of principles, 2:230-233, 2:236, 2:241, 2:248
National Conference on Professional Ethics, 2:446
National conferences on state legislation, 2:337
National Education Association, 1:332
National Guard, 2:44
National Industrial Conference Board, 2:382
National Merit Scholarship, 2:307, 2:308
National Society of Public Accountants, 2:328-329, 2:331, 2:343
negotiations with, 2:334-337
Natural Business Year Council, 1:150
Nau, Carl H., 1:125
Naval Consulting Board, 1:141
Navy Department, 2:44, 2:45
Needham, James J., 2:384
"New Approaches to Public Education," 2:381
New Jersey Society of Certified Public Accountants, 1:59
Newsletters, "canned," 2:460-461
Newsom, Earl, 2:240, 2:243, 2:379, 2:392
Newsom, Earl & Company, 2:240, 2:379, 2:380
New York Board of Examiners of Public Accountants, 1:30
New York Conference of Lawyers and Certified Public Accountants, 2:220
New York County Lawyers Association, 2:219-220
New York Court of Appeals, 2:220
New York Life Insurance Company, 1:30
New York School of Accounts, 1:41
New York Society of Security Analysts, 2:106
New York State Chamber of Commerce, 2:399
New York State Department of Education, 1:104, 2:265
New York State Society of Certified Public Accountants, 1:30, 1:42,

1:50, 1:57, 1:184, 1:185, 1:192, 1:195, 1:199, 1:255, 1:335, 1:354, 1:355, 2:52, 2:151, 2:184, 2:219, 2:220, 2:235, 2:324
see also McKesson & Robbins case
New York Stock Exchange, 1:144, 1:158, 1:160-180 *passim*, 1:182, 1:183, 1:203, 1:354, 2:5 2:10, 2:20, 2:69, 2:80, 2:88, 2:90, 2:139, 2:143, 2:151, 2:153, 2:277, 2:387
Committee on Stock List, 1:164, 1:165, 1:175, 1:177, 1:178
concern about accounting practices, 1:160-161
correspondence on accounting principles, 1:174-180
requirement for audits, 1:169
see also McKesson & Robbins case
New York Times, The, 1:41, 1:88, 2:105
New York University, 1:260
School of Commerce, Accounts and Finance, 1:30, 1:42, 1:97, 1:99
New York World Telegram, 2:25
Nicholson, J. Lee, 1:143, 1:311
Nissley, Warren W., 1:276, 2:12, 2:13, 2:300-301, 2:302
Niven, John B., 1:51, 1:120, 1:335, 1:339, 1:340, 1:343, 1:347
Non-Partisan Tax Commission, 2:398-400
Non-profit organization, independence rule related to service as director, 2:458
North, Raymond E., 2:287
Notes receivable, *see* Accounts receivable
Noyes, Charles E., 2:305-306, 2:359

Objectives of AICPA, 2:501-503
Office of Price Administration, 2:85
Office of Procurement and Material, 2:45
Ohio Society of Certified Public Accountants, 2:9
Ohio State University Institute on Accounting, 2:184
"Old Myths and New Realities in Accountancy," (Briloff), 2:197
Oliphant, Walter J., 2:498
Olive, George S., 2:46, 2:51
Olive, Geo. S. & Company, 2:46
O'Mahoney, Senator, 2:213
Operations research, 2:54-55
Opinions, auditors', 2:151-158
see also Committee on professional ethics
Oregon Agricultural College, 1:271
Organizations, Institute relationships with other, 2:488-490
Otterbourg, Edwin M., 2:219
"Co-operation Between Lawyers and Accountants in Tax Practice," 2:235
Ould, James P., 2:383
Owen, George, 2:289
Oxford University, 2:151, 2:263

Pace, Homer S., 1:297-300 *passim*, 1:312
Pace College, 1:43, 1:297
Pace Institute of Accountancy, 1:43, 1:297
Pacioli, Fra Luca, *Summa de Arithmetica Geometria Proportioni et Proportionalita*, 1:14
Pan American Union, 2:372
Panic of 1907, 1:54-55
Papworth, William, 2:359
Parnell, Roderic, 2:363
Paton, William A., 1:214, 1:261, 1:262, 1:267, 1:301, 2:13, 2:288
Corporate Profits as Shown by Audit Reports, 1:301
Introduction to Corporate Accounting Standards, An (with A. C. Littleton), 2:16
Pattinson, I. Graham, 2:484n
Pearl Harbor, 2:45-46
Pecora, Ferdinand, 1:167-168
Pecora investigation, 1:167-169
Peloubet, Maurice E., 2:77, 2:288, 2:320n
Penney, Louis H., 2:77, 2:342, 2:343, 2:345

Pennsylvania Association of Public Accountants, **1**:51
Pennsylvania Board of Examiners of Public Accountants, **1**:104
Pennsylvania Institute of Certified Public Accountants, **1**:51, **2**:30, **2**:490
"people's capitalism," **2**:57
Perry, Donald P., **2**:264-265, **2**:320n
Personal liability, unlimited, **2**:472-473
Personnel
  accounting, **1**:151-154
  attracting competent, **2**:299-300
  recruiting activities, **2**:305-310
  testing program, **2**:300-304
Petroleum Administration for War, **2**:421
Phi Beta Kappa, **1**:271
Phillips, J. A., **2**:414n
Philosophy of Accounts, The (Sprague), **1**:102
Philosophy of Auditing, The (Mautz and Sharaf), **2**:192
"piecemeal" approach to accounting principles, **2**:18
Pierson report, **2**:273-276
"Plan for International Peace, A" (Sells), **1**:140
Planning
  committee, **2**:496
  for the Institute, **2**:497-503
  for the profession, **2**:495-497
"Plan of Co-operation in the Conduct of Examinations," **1**:273
Plender, Lord, **1**:310
Policy changes on education and experience requirements, **2**:280-285
Post Office Department, **2**:430
Poulson, Norris, **2**:383
Powell, Weldon, **2**:92, **2**:95, **2**:111
Practice in corporate form, **2**:468-475
  audit companies, **2**:468-469
  data-processing services, **2**:470-471
  service bureaus, **2**:469
Practice review, **2**:455-456
Practice review committee, **2**:169-170, **2**:455
Practice units, **1**:149
"Practitioners Forum," **2**:363
"Press Publicity and How To Get It," **2**:376
Price-level accounting, **2**:68-70
Price-level depreciation, **2**:68
Price Waterhouse & Co., **1**:27, **1**:28, **1**:30, **1**:51, **1**:131, **1**:133, **1**:136, **1**:163, **1**:175, **1**:189, **1**:201, **2**:68, **2**:92, **2**:133, **2**:208, **2**:230, **2**:372, **2**:486, **2**:499
  see also McKesson & Robbins case
Priorities and Allocations Board, **2**:48
Profession
  characteristics of a, **2**:266
  seven criteria, **1**:3
Professional Accounting in 25 Countries, **2**:371
"Professional and Technical Practitioners in Accounting" (Trueblood), **2**:491
Professional corporation, resolution on, **2**:473-474
Professional development program, **2**:296-299
  Board of Managers, **2**:296, **2**:297
Professional ethics, **1**:84-87
  see also Committee on professional ethics; Rules of professional conduct
Professional Ethics of Certified Public Accountants, **2**:448
Professional Ethics of Public Accounting, **2**:448
"Professional Help Wanted," **2**:307
"Professional Relations of Lawyers and Certified Public Accountants," **2**:253
Professional service associations, **2**:471
"Profile of the Profession: 1975," **2**:493
Profit-and-loss statement, in registration statement, **1**:190-191
Profit, unrealized, **1**:176
pro forma financial statements, **1**:295
Promotion, publicity, and encroachment, **2**:460-465
  see also Advertising
Proprietary schools, rules of conduct on, **1**:246

"Protection of Investments," 1:293
Psychological Corporation, 2:304
"Public Accountant and the Credit Man, The" (Hunter), 1:291
"Public Accounting as a Career," 2:305
Publications, 2:359-360
Publications program, 1:304
Publicity, 1:297-301
  in the press, rule on, 2:463-464
"Public Interest in Accountancy" (Berle), 1:172-173
Public Law 4, 79th Congress, 2:423, 2:424
Public Law 248, 79th Congress (Government Corporation Control Act), 2:423
Public Law 863, 84th Congress, 2:430
Public relations, 1:301-302, 2:350-351
  early efforts, 2:375-380
  later efforts, 2:380-382
  program and policy, 2:391-392
  public service and, 2:374-394
"Public School Costs: An Accounting Primer for School Board Members and Taxpayers," 2:381
Public service, 2:382-384
  public relations and, 2:374-394
Public Utility Holding Company Act of 1935, 2:60
"Public Warehouses—Controls and Audit Procedures for Goods Held," 2:171

Qualified certificates, 1:82-83
"qualifying body," emergence of, 1:118
Quality control, voluntary, in auditing, 2:368
Quartermaster Corps, 2:44
Queenan, John W., 2:238, 2:239, 2:240, 2:246, 2:251, 2:254, 2:262, 2:354,
Quigley, William R., 2:421

Ramsey County Bar Association, Minnesota, 2:223, 2:233
Rand, Waldron H., 1:97, 1:119, 1:125, 1:218-219, 1:236
Randall, John D., 2:222, 2:226-234 *passim*
Reciprocity, 1:287-288
Reckitt, Ernest, 1:51
Recollections of the Early Days of American Accountancy 1883-1893 (Anyon), 1:26n
Reconstruction Finance Corporation, 2:422, 2:423
Recruiting activities, personnel, 2:305-310
"Red Book" ("Audits by Certified Public Accountants"), 2:163
Reed, Congressman, 2:401
Reed Bill, 2:247
Referrals, rule on, 2:462-463
Registration statement, financial statements to be filed with, 1:190-191
Regulation S-X, *see* Securities and Exchange Commission
Regulation under state law, 1:279-289
Regulatory legislation, 2:322-325
  two-class, 2:332-333
Related occupations, rule on, 2:476-477
"Relationship Between the Practice of Law and Accounting" (Byerly), 2:212
"Relationship of the Banker to the Public Accountant, The" (Cannon), 1:103
"Reliance on Other Auditors," 2:371
Renegotiation, 2:49
"Reporting of Leases in Financial Statements of Lessee," 2:140
"Reporting the Results of Operations," 2:141
"Report of the Standing Committee on Accounting Education," 2:283
Report on Investigation of the Securities and Exchange Commission in the Matter of McKesson & Robbins, 2:23

Reports
auditors', **2**:151-158
standard form of, **1**:178-179
Report writing, course in, **2**:293
Research division, **2**:95
Research project on cost accounting principles, **2**:438
Responsibility and legal liability, **1**:80-82
"Responsibility of Auditors" (Rose), **1**:252
Restrictive legislation, **1**:282-286
Reunion of accounting organizations, **1**:353-371
Revenue Act of 1924, **1**:222
Revenue Act of 1942, **2**:49, **2**:213, **2**:222
Revenue Act of 1962, **2**:98
"Revised SEC Rule on Accountants' Certificates, The," **2**:38
Reynolds, Senator, **1**:185-190 *passim*
Reynolds, W. B., **1**:138
Duties of the Junior Accountant, The (with F. W. Thornton), **1**:138, **1**:305
Rich, Wiley Daniel, *Legal Responsibilities and Rights of Public Accountants,* **1**:306
Richardson, A. P., **1**:100, **1**:114-115, **1**:125, **1**:131, **1**:299, **1**:305, **1**:309, **1**:348, **1**:370-371
Ethics of a Profession, **1**:305
Richardson, Mark E., **2**:288, **2**:414n, **2**:479-480
Ring, John R., **2**:118, **2**:484
Ripley, William Z., **1**:161-162, **1**:170, **1**:182, **1**:191
Main Street and Wall Street, **1**:161
Rockefeller Foundation, **2**:68
Rockwood, Charles P., **2**:274-275
Ronald Press Company, **1**:101, **1**:306
Roosevelt, Franklin D., **1**:170, **1**:181, **2**:42
Roosevelt, Theodore, **1**:24, **1**:55-59 *passim*
Rose, Bernard, **1**:252-253
"Responsibility of Auditors," **1**:252
Rose, H. Chapman, **2**:251
Ross, Adam A., **1**:33, **1**:125
Ross, T. Edward, **2**:261
Roy, Robert H., **2**:276
Horizons for a Profession (with others), **2**:277-286 *passim,* **2**:314
Rules of professional conduct, **1**:229-230, **1**:231-232, **2**:441-442, **2**:456
advertising, **1**:230-234, **2**:460, **2**:461-462
audit companies, **2**:468-469
commissions from the laity, **1**:245-246
competitive bidding, **1**:243-244, **2**:465-468
confidential relationship, **2**:475-476
contingent fees, **1**:234-237, **2**:476
disclosing departure from opinions of APB, **2**:453-454
employment offers, **1**:234
enforcement, **1**:247, **2**:442
house organs, distribution of, **2**:461
incompatible occupations, **1**:246
incorporation to offer EDP services, **2**:470-471
mixed partnerships, **2**:477-478
No. 2, **1**:237-239, **2**:450
No. 5, **1**:246, **2**:450
No. 12, **2**:452
No. 13, **2**:186-191
overhaul of, **2**:448-449
proprietary schools, **1**:246
publicity in the press, **2**:463-464
referrals, **2**:462-463
related occupations, **2**:476-477
responsibility to investors, **1**:237-239
service bureaus, **2**:469
solicitation, **2**:462, **2**:468
technical standards, **2**:449-455
utilizing the work of other CPAs, **2**:452-453
see also Code of professional ethics; Independence
Rural Electrification Administration, **2**:437
Russell, Donald M., **2**:484n
St. Louis Breweries Ltd., **1**:28

Sales, disclosure of, **1:196**
Salowe, William, **2:298**
Sanders, Thomas H., **2:13**, **2:14**, **2:16**, **2:46**, **2:288**
"Statement of Accounting Principles, A" (with Hatfield and Moore), **2:13**
Savings and loan audits, **1:211**
Savoie, Leonard, **2:390-391**, **2:499**
Schackne, Stewart, **2:392**
Schism in accounting organizations, **1:303**, **1:314-352**
Schlosser, Robert, **2:281**, **2:298**
Schlude, **2:403**
Schneeman, Donald, **2:484n**
School of Commerce, Accounts and Finance (Boston), **1:98**
Schulte, Arthur A., Jr., **2:194-195**, **2:197-200** *passim*
"Compatibility of Management Consulting and Auditing," **2:194**
Scobie, John C., **1:131**
Scovell, Clinton H., **1:147**
Scovill, Hiram T., **1:261**, **2:69**, **2:288**
Search for Accounting Principles, The (Storey), **2:13**
Seaview Symposium, **2:142-143**
Securities Act of 1933, **1:154**, **1:168**, **1:173**, **1:179**, **1:182-193**, **1:355**, **2:176**
administration of, **1:193**
audit provision, **1:184-193**
financial statements to be filed with registration statement, **1:190-191**
Securities and Exchange Commission, **1:182**, **1:198**, **1:205**, **1:263**, **2:5**, **2:9**, **2:16**, **2:21**, **2:59**, **2:69**, **2:81**, **2:86**, **2:100**, **2:101**, **2:125**, **2:148**, **2:165**, **2:173**, **2:200**, **2:341**, **2:443**, **2:494**
authority to prescribe accounting rules, **1:191-192**, **1:193**
chief accountant's office created, **1:199**
influence on auditing standards, **2:155-158**
Institute and, **1:194-196**
observations from, **2:122-124**
position on investment credit, **2:105-110**
pressure for comparability, **2:130-132**
pressure for uniform accounting principles, **2:60-65**
Regulation S-X, **2:67**, **2:148**, **2:157**, **2:182**
rules on independence, **2:176-177**
see also Accounting Series Releases; McKesson & Robbins case
Securities Exchange Act of 1934, **1:154**, **1:168**, **1:180**, **1:193-194**
Seidemann, H. P., **2:419**, **2:424**
Seidman, J. S., **2:77**, **2:118**, **2:130**, **2:140**, **2:354**, **2:414n**, **2:486**, **2:490**
"What Is the Future of the Accounting Profession?" **2:490**
Selective Service Act, **2:44**
Selective Service System, **2:47**
Sells, Elijah Watt, **1:30**, **1:51**, **1:56**, **1:59**, **1:119**, **1:121**, **1:125**, **1:137**, **1:140**, **1:275**
"Plan for International Peace, A," **1:140**
Sells medal, **1:275-276**
Seminars for financial writers and editors, **2:390-391**
Senate Committee on Banking and Currency, **1:167-169**, **2:424**
testimony of Arthur H. Carter, **1:185-190**
Senate Committee on Expenditures in the Executive Department, **2:405**
Senate Finance Committee, **2:399**, **2:400**, **2:403**, **2:407**
Senate Judiciary Committee, **1:226**, **2:213**, **2:228**, **2:256**
Senate Select Committee to Investigate the Executive Agencies of the Government, **2:419**
Service bureaus, **2:469**
Shapiro, Morris, *see Agran, Reuben, CPA* v. *Morris Shapiro et al.*
Sharaf, Hussein A., *The Philosophy of Auditing* (with R. K. Mautz), **2:192**
Sherman Antitrust Act, **1:24**, **1:55**
Shorrock, E. G., "Should Accountants Advertise?" (with Cooper and Gore), **1:91-92**

"Should Accountants Advertise?" (Cooper, Gore, Shorrock), 1:91-92
Simonetti, Gilbert, 2:414n
Simpson, W. Kenneth, 2:320n
Sixty Million Jobs (Wallace), 2:56
Slaughter, R. H., 2:420
Small Business Administration, 2:437
Small firms, *see* Accounting firms
Smith, Alexander, 1:77-78, 1:79
  "The Abuse of the Audit in Selling Securities," 1:77-78
Smith, Alfred E., 1:284, 2:323
Smith, Charles W., 2:69
Smith, Frank P., 2:265
Smith, Fred B., 2:481
Smith, Robert M., 2:360
Smith v. *London Assurance Corp.*, 1:250
Social Science Research Council of America, 1:171
Society of Accountants, 1:19
Society of Investment Analysts, 2:105
Solicitation, rule on, 2:462, 2:468
"Some Evils of Competition," 1:293
Spacek, Leonard, 2:74-77, 2:92, 2:104, 2:108, 2:125-126, 2:127-128
Special committee, 2:117-118
  recommendations, 2:119-122
"Specialization," 2:478
Specialized knowledge, *see* Common body of knowledge
Sprague, Charles Ezra, *The Philosophy of Accounts*, 1:102
Springer, Durand W., 1:327-332 *passim*, 1:338, 1:368-371 *passim*
Sprouse, Robert T., "A Tentative Set of Broad Accounting Principles for Business Enterprises" (with M. Moonitz), 2:97
Staats, Elmer B., 2:431
Staff training, 2:288-289
Staggers, Harley O., 2:109
Standard Oil Company (New Jersey), 1:59, 1:71, 2:392
Standards of competence, 1:260-278
  see also Auditing standards and procedures
Stanford University, 2:438
Stans, Maurice H., 2:73, 2:118, 2:244, 2:245, 2:287-290 *passim*, 2:383
Starkey, Rodney F., 1:201, 2:40
"Statement of Accounting Principles" (Sanders, Hatfield, and Moore), 2:13
"Statement of Accounting Principles Underlying Corporate Financial Statements," 2:64
Statement of auditing standards, 2:155
Statement of Principles Relating to Practice in the Field of Federal Income Taxation, 2:252
"Statement of Source and Application of Funds, The," 2:139
Statements on Auditing Procedure
  No. 1, 2:35, 2:41
  No. 23, 2:160-161, 2:162, 2:187, 2:379, 2:451, 2:455
  No. 33, 2:163
  No. 41, 2:172, 2:476
"Statements on Management Advisory Services," 2:483
"Statements on Responsibilities in Tax Practice," 2:413, 2:481
State regulation, 1:279-289
State societies, relations with Institute, 1:320-321, 2:345-349
"Status of Accounting Research Bulletins," 2:141
"Status of Pronouncements of Accounting Principles Board," 2:112
Staub, Walter A., 1:51, 1:173-174, 1:175, 1:354-356, 1:358, 2:19, 2:84, 2:288
Stempf, Victor H., 2:52, 2:216, 2:414n
Sterrett, Joseph E., 1:51, 1:74, 1:82, 1:86, 1:113, 1:119, 1:125, 1:130, 1:142, 1:143, 1:250, 1:251, 1:310, 1:316, 1:336
Stevens, Richard F., 1:42
Stewart, Andrew, 2:45
Stewart, J. Harold, 2:46, 2:67, 2:69, 2:430
Stock-market crash, 1:164-166
Stone, Marvin L., 2:356, 2:472
Storey, Reed, 2:13, 2:17, 2:18, 2:140

The Search for Accounting Principles, **2**:13n, **2**:17
Subcommittee on Internal Revenue Taxation, **2**:407
"Subsequent Discovery of Facts Existing at the Date of the Auditor's Report," **2**:172
Suffern, Edward L., **1**:71
Summa de Arithmetica Geometria Proportioni et Proportionalita (Pacioli), **1**:14
Surplus
capital, **1**:176
earned, **1**:158-159, **1**:176
Surrey, Stanley S., "The Congress and the Tax Lobbyist—How Special Tax Provisions Get Enacted," **2**:411-412
Sweet, Homer N., **2**:484n
Symposium on Corporate Financial Reporting (Seaview Symposium), **2**:142-143
System Magazine, **1**:150
Systems Development Corporation, **2**:364

Taft, William Howard, **1**:55, **1**:296, **2**:415
Tax accounting, business accounting and, **2**:400-403
Tax Adviser, The, **2**:360, **2**:413
Taxation, general policy on, **2**:409-412
Tax Commission, Non-Partisan, **2**: 398-400
Tax committee, **2**:395-414
Tax Court bill, **2**:221-222, **2**:226, **2**:228-229
Tax Foundation, **2**:399
Tax legislation and regulations, **2**:406-409
Taxpayers, representation of, **2**:212-214
Tax practice, **1**:213-227
course in administration of, **2**:293
defense of, **2**:204-257
disagreement with American Bar Association over, **1**:224-227, **2**:206-257
ethical problems, **1**:218-219
growing complexities, **1**:218-219
responsibilities in, **2**:479-481
Tax practice dispute
appeals to federal government, **2**:225-226
appeal to Congress, **2**:242
appeal to public, **2**:242-243
appeal to Treasury Department, **2**:241-242
Treasury Department action, **2**:251-253
Tax returns
attestation of, **1**:215-216
extensions for filing, **2**:397-398
Tax system, toward a viable, **2**:395-414
Taylor, Frederick Winslow, **1**:147
Technical activities during World War II, **2**:49-50
Technical Amendments Bill, **2**:407
Technical tax advice, **2**:404-405
Teele, Arthur W., **1**:143
"Telling the School Costs Story," **2**:381
Temple University Accounting Forum, **2**:125
Temporary National Economic Committee, **2**:56
Tennessee Supreme Court, **2**:323, **2**:324
Tennessee Valley Authority, **2**:421, **2**:422
"Tentative Set of Broad Accounting Principles for Business Enterprises, A" (Mooney and Sprouse), **2**:97
"Tentative Statement of Accounting Principles Affecting Corporate Reports," **2**:9, **2**:16
"Tentative Statement of Auditing Standards—Their Generally Accepted Significance and Scope" (Kracke and others), **2**:148, **2**:179, **2**:181
Terminology, accounting, **1**:76-77, **1**:206
Testing program, personnel, **2**:300-304
Texas Society of Certified Public Accountants, **2**:377
Texas State Board of Public Accountancy, **2**:166, **2**:167

Third-party liability, **1**:252
Thornton, F. W.
Duties of the Junior Accountant, The (with W. B. Reynolds), **1**:138, **1**:305
Duties of the Senior Accountant, **1**:306
Financial Examinations, **1**:306
"Too Many Annual Reports Still Are Guessing Games," **2**:73
Treadway, Representative, **2**:398
Treasury Department, **1**:69, **2**:97, **2**:205, **2**:213, **2**:224, **2**:225, **2**:226, **2**:235, **2**:237, **2**:250-253, **2**:395, **2**:396, **2**:399, **2**:402, **2**:403, **2**:404, **2**:412, **2**:417-423 *passim*, **2**:429, **2**:481
action in tax practice dispute, **2**:251-253
appeal to, in tax practice dispute, **2**:241-242
Circular 230, **1**:220, **1**:236, **2**:209, **2**:239, **2**:241, **2**:247, **2**:250, **2**:445
Committee on Enrollment and Disbarment, **1**:220, **2**:445
Treasury stock, dividend on, **1**:176
Trial Board, **2**:442, **2**:444, **2**:447
Troper, Morris C., **2**:45
Trueblood, Robert M., **2**:128-130, **2**:353, **2**:383, **2**:433, **2**:490, **2**:495, **2**:497
"Management Service Function in Public Accounting, The," **2**:491
"Professional and Technical Practitioners in Accounting," **2**:491
Trump, Guy W., **2**:280, **2**:281, **2**:298, **2**:308
Trust-busting, **1**:59-60
Truth in Securities Act, **1**:161, **1**:182, **1**:183
Tucker, Arthur R., **1**:299, **1**:300, **1**:312-313
"two-class law," **1**:283-284

Ultramares, **1**:255-259, **2**:152
Unauthorized Practice News, The, **2**:222, **2**:235
Uniform accounting, **1**:129-135
"Uniform Accounting"
see "Approved Methods for the Preparation of Balance Sheet Statements"
Uniform accounting principles, SEC pressure for, **2**:60-65
Uniform CPA Examination, **1**:271-275, **1**:370
Uniformity, **2**:88
vs. flexibility, **2**:127
see also Comparability
United States Steel Company, **1**:6, **1**:28, **1**:29, **1**:80, **1**:165
auditor's certificate (1903), **1**:28-29
United States Tax Court, **2**:213, **2**:228, **2**:238, **2**:243, **2**:247, **2**:255
University of California, **2**:289
University of Chicago National Opinion Research Center, **2**:308
University of Michigan, **2**:263, **2**:265
Bureau of Business Research, **2**:265
University of Pennsylvania
Evening School of Accounts and Finance, **1**:100
Wharton School of Commerce and Finance, **1**:42, **1**:51, **1**:97
University of the State of New York, **1**:41
Unjust claims, protection against, **2**:173-174
Unrealized profit, **1**:176

VanderLaan, James, **2**:498
van Dien, E., **1**:310
"Verification of Financial Statements," **1**:159, **1**:178, **2**:20
Veterans Administration, **2**:287
Veysey, W. H., **1**:38
Vigorito, Joseph, **2**:383
Vollum, C. M., **1**:111-112

Wagner, Senator, **1**:186, **1**:226
Waldo, Earl A., **2**:484n
Waldorf-Astoria Hotel, **2**:1

Wallace, Henry, **2**:57
  Sixty Million Jobs, **2**:56
Wall Street Journal, **1**:115, **2**:105, **2**:137, **2**:138, **2**:166, **2**:389
Walter, Francis E., **2**:228
Walter Bill, **2**:248
Walton, Seymour, **1**:76
War Committee, Institute, **1**:142
War Department, **2**:44, **2**:45, **2**:48-49
War Manpower Commission, **2**:47, **2**:50
War Production Board, **2**:46, **2**:48, **2**:49
Warren, Lindsay C., **2**:419, **2**:424, **2**:431
Washington Law Review, **2**:138
Washington Society of Certified Public Accountants, **1**:225
Webster, Norman E., **1**:25, **1**:275
  American Institute of Public Accountants — Its First Twenty Years, **1**:25n
Weiss, William F., **1**:120, **1**:125
Wellington, C. Oliver, **2**:43, **2**:45, **2**:213, **2**:288
Welsch, Glenn A., **2**:118
Werntz, William W., **2**:17, **2**:29, **2**:62-69 *passim,* **2**:89, **2**:93, **2**:117-118, **2**:146-147, **2**:157, **2**:288
West, William H., **1**:164
Westinghouse Electric and Manufacturing Company, **1**:146
Wharton School of Commerce and Finance, **1**:42, **1**:51, **1**:97, **1**:260
"What *Are* Earnings? The Growing Credibility Gap," **2**:136
"What Is the Future of the Accounting Profession?" (Seidman), **2**:490
Whitney, Jack M. II, **2**:105-106
Wickersham, George W., **1**:64
Wilcox, Edward B., **2**:69
Wilcox, Frank L., **2**:383, **2**:484n
Wildman, John R., **1**:99, **1**:262, **1**:265-266, **1**:271
Wilkinson, George, **1**:49, **1**:124
Wilkinson, Theodore L., **2**:372
Williams, C. B., **1**:311
Williams, T. Dwight, **2**:287
Willis, Representative, **2**:257
Wilson, Woodrow, **1**:55
Wisconsin State Board of Accountancy, **1**:199
Wisconsin State Board of Public Affairs, **1**:199
Wisconsin Tax Commission, **1**:199
Wise, Tom, "The Auditors Have Arrived," **2**:386-389
Witschey, Robert E., **2**:100-102, **2**:110, **2**:112, **2**:290, **2**:335, **2**:337, **2**:350, **2**:486, **2**:490
  "The Accounting Function for Small Business," **2**:490
Women in accounting, **1**:153-154
Wood, Ben, **2**:301, **2**:302
Woodside, Byron D., **2**:106-107, **2**:122-124
Working with the Revenue Code, **2**:413
World War II, **2**:16-19, **2**:42-55
  accounting manpower, **2**:46-48
  aftermath, **2**:52-55
  consulting activities, **2**:48-49
  defense preparations, **2**:43-44
  Pearl Harbor, **2**:45-46
  technical activities, **2**:49-50
Wright, Loyd, **2**:246

Yalden, James, **1**:38, **1**:39
Yates, Frank L., **2**:424
Yeager, Ford & Warren, **2**:496
Yearbook, **1**:76, **1**:115, **1**:127, **1**:159, **1**:239, **1**:244, **1**:265, **1**:304, **1**:324, **1**:343, **2**:50, **2**:443
Year-end audits, **1**:149-151
Young, Arthur, **1**:63
Young, Arthur & Company, **1**:63, **1**:154, **1**:276

Zebley, John H., Jr., **2**:287, **2**:288, **2**:320n, **2**:484n