Accounting Historians Journal

Volume 10
Issue 2 *Fall 1983*

Article 10

1983

Book reviews [1983, Vol. 10, no. 2]

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The Accounting Historians Journal
Vol. 10, No. 2
Fall 1983

BOOK REVIEWS

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Howard F. Stettler, Editor, *Auditing Looks Ahead—Proceedings of the 1972 Touche Ross/University of Kansas Symposium on Auditing Problems* (Lawrence, Kansas: School of Business, University of Kansas, 1972, pp. 135, $5.00).

Reviewed by
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Auditing Looks Ahead includes eight invited papers and seven discussants' responses presented at the first Touche Ross/University of Kansas auditing symposium. Since 1972, these symposia have been held biennially. As of this writing there have been five proceedings published, and with a sixth symposium presented in May 1982. The papers and discussions at the first symposium were concerned with contemporary auditing problems of 1972 vintage. The basic problems presented and discussed at the first symposium are like good wines, in that age (ten years) has not eliminated the problems but has just changed their flavor. Thus, someone involved in a current auditing problem or an historian interested in a quick overview of a problem as it existed in 1972 might benefit from reading one of the presentations or discussions given at the 1972 Touche Ross/University of Kansas Symposium. Because so much has changed in ten years, and these papers cover descriptive research of the state of the art, I have attempted to summarize, sometimes by giving little more than the title of the paper, and only minor evaluation, if any, of the paper's contribution to the profession, as might ordinarily be done in a book review.

R. G. Brown and Roger H. Salquist in "Some Historical Auditing Milestones; An Epistemology of an Inexact Art" attempt to order the evolutionary process of the history of auditing by describing audit milestones classified by era, e.g., emergence era, and then by socio-econo-technological influences, e.g., industrial revolution. Their objective of attempting to give order to the evolutionary process which has shaped the present state of the art, may have been and still may be an impossible task, especially in a short article. Horace G. Barden, as discussant, correctly pointed out that Brown and Salquist missed some important milestones and different people have different opinions as to the importance of past auditing events. The value of Brown and Salquist's attempt to pinpoint the milestones in auditing is that it is a springboard that others in the field can use in order to obtain a quick overview of auditing milestones, and a starting point for more comprehensive search for milestones and reasons.

In "What Are the Courts Saying to Auditors?" A. A. Sommer provides an excellent summary of common law developments, statutory laws, and recent important common law cases involving the auditor's liability, through 1972. Of course, like all problems of 1972 vintage, auditors continue to audit and the courts continue to render opinions concerning the auditors' duties and responsibilities. Today, updated versions of most of what Mr. Sommer discussed are found in any good auditing textbook.

Kenneth W. Stringer's paper, "Toward Standards for Statistical Sampling," summarizes the AICPA's Committee on Auditing Procedure work that led to Appendix B of SAP No. 54, which later became codified in SAS No. 1, Section 320, Appendix B, *Precision and Reliability for Statistical Sampling in Auditing,* and finally has been superseded in 1982 by SAS No. 39, "Audit Sampling." Discussant James W. Kelley questions the need to perform compliance tests of internal control procedures and implies one might perform a more efficient audit by not relying on the internal control system and using a high confidence level (e.g., 95%) in the performance of substantive tests instead of a lower confidence level, if the auditor were to rely on internal control as SAP No. 54 suggests. Kelly's point, not performing compliance testing and thereby not relying on internal control, has finally been formally recognized some ten years later (August 1982) in SAS No. 43, "Omnibus."

In "Future Extensions of Audit Services; Meeting Investors' Future Needs" Donald J. Bevis discussed the need for public companies to publish forecast data in order to meet investors' needs. Despite his enthusiasm and cry for speed, implementation of forecasts has not to date emerged. Few, if any, annual reports carry forecast data.

In "Toward Standards for Materiality (?)" William Holmes suggests a practical alternative to defining materiality, which he believes should be left to courts. Mr. Holmes' alternative to defining materiality is for the profession to establish a standard of "significant distortion." Significant distortion occurs when financial statements *per se* might cease to be "fair." Sam M. Woosley discusses Holmes' paper by suggesting a framework for defining materiality. Both Mr. Holmes, before the 1972 proceedings, and Mr. Woolsey, after the 1972 proceedings, had articles on this topic in the *Journal of Accountancy*.

"Toward a Philosophy of Auditing" by R. K. Mautz offers some thoughts on (1) to whom are auditors responsible and (2) for what are auditors responsible. Mautz concludes that neither management nor the general public is the auditor's client. An auditor should "steer a course that gives proper respect to the relative rights of the several interests in the auditor's work. . . ." Mautz concludes that the client relationship between an auditor and shareholder is strongest since shareholders have the greatest relative interest, while it is weakest between auditor and the general public. Mautz then discusses for what are auditors responsible by concluding that the auditors are responsible for not only technical competence, but also what he defines as "social competences."

In "Future Directions for Auditing Research" Douglas R. Carmichael attempts to summarize auditing research as it relates to various research methods, and to give examples of auditing research. He suggests that empirical research with data from real practice situations, excluding surveys, and not abstract data, is most needed in the profession.

He outlines three areas where research in auditing appears to be important. These are: (1) expansion of the attest function, (2) refinement of auditing methods, and (3) professional responsibilities. Frederich Newmann's response to Mr. Carmichael's paper is that the usefulness of auditing theory drawn from practice is difficult because of the difficulty of isolating a variable, and may be illusory because practice is inconsistent, unorganized, and unsystematic in its approach to problems. Newmann suggests greater cooperation and joint research ventures between academicians and practitioners.

Finally, Marvin L. Stone's dinner address, "The Problem with Auditing Is . . . (The Stuff Dreams are Made Of)," is an entertaining scenario of dreams about Marvin as an expert witness who, in one dream, explains what the SEC and an auditor do by comparing them to football officials, with the SEC having the whistle, and the players being audited public companies.

Since Symposium I is now over ten years old, it gives historians a glimpse at what some of the leading auditing academicians and practitioners of 1972 thought were the contemporary auditing issues then and their opinions as to how these issues might be resolved.

Charles William Lamden, *The Securities and Exchange Commission: A Case Study in the Use of Accounting as an Instrument of Public Policy* (New York: Arno Press, 1978, pp. 353, $31.00).

Reviewed by
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Charles William Lamden completed *The Securities and Exchange Commission: A Case Study in the Use of Accounting as an Instrument of Public Policy* in 1949 as a part of his requirements for the degree of Doctor of Philosophy. As the title indicates Lamden intended to discuss the use of accounting in public policy. While he referred to the active and passive use of accounting he did not present a convincing argument for or against the use of accounting as an instrument of public policy. Neither did he demonstrate very well how it has been used in this way. However, Lamden did present an excellent history of the early issues confronted by the SEC and the accounting profession.

This book includes eleven chapters, most of which relate to one of three areas:

1. Early standard-setting process with and without the SEC.
2. Major issues confronting the profession during the late 1930s and the 1940s.
3. Significant areas of controversy on which the profession and the SEC sometimes disagreed.

Chapters related to the first area remind the reader that the profession has been and continues to be self-regulating and frequently takes the initiative in problem solving and standard setting. Many of the major issues discussed by Lamden continue to be major issues today and controversies between the profession and the SEC may not have been resolved.

As one progresses through *The Securities and Exchange Commission* he is alternately impressed by the tremendous progress and the lack of progress by the accounting profession. Within three pages, both conclusions can be drawn. In Chapter VII, Lamden reviewed the SEC requirements for financial statement presentation.

When discussing the requirements for the presentation of "surplus" he explained:

> If a separation can be made the amount of the paid-in surplus and revaluation surplus should be shown separately. If the separation cannot be made, it must be explained that the capital surplus is composed of paid-in, revaluation, or other types of surplus if such is the case. (p. 164)

Today this issue is solved. Not only has the profession eliminated the use of the word surplus, but it has also required that this "surplus" be properly labeled and separately reported according to source.

A short time later, Lamden discussed the concept of writing up assets to current appraised values. He explained:

> The Commission has also expressed itself as to the permissibility of increasing the surplus by appraising the assets on the balance sheet. Such appraisals are permitted if good reason can be shown for them, but the surplus arising from such revaluations must be stated separately and not included with the capital or earned surplus . . . (p. 166)

Current efforts to develop current value accounting measures sometimes confuse historical retained earnings and the effects of revaluations. The reader wonders about the pace and direction of progress when he is reminded of these 1940 issues and then he compares them to the partial solutions of today.

Lamden's book is replete with examples of this type. The modern day reader is never quite sure whether the accounting profession has progressed in its search for accounting principles or whether it has gone in circles. Sometimes it appears that the movement has been in the direction of short side trips. As one reads Lamden, he is reminded of the old adage that "the more things change, the more alike they are."

Because of this enlightening perspective of viewing accounting standard setting in light of its beginning and its current status, I highly recommend that anyone interested in the standard-setting process or progress therein read Lamden's *The Securities and Exchange Commission*.

David A. R. Forrester, *Issues in Accountability No. 4: Legislation in Process, The Belgian Accounting Revolution and its Preparation* (Glasgow: Strathclyde Convergencies, 1980, pp. 48, £ 3).

Reviewed by
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Issue No. 4 of the series, *Issues in Accountability,* discusses the process of establishing the reformed accounting legislation in Belgium. It comprises, as the subtitle indicates, "A study of background and detail with reference to Annual Accounts, Holding Companies and Accounting Plans."

In his "Introduction" the author briefly explicates the situation of Belgium and explains some of the reasons why this case is worth consideration.

The next chapter discusses the historical background illustrating *inter alia* the importance of the accounting analysts, the Belgian economic history, the Belgian enterprises, the financial situation, the organization of the economy, the stock exchanges (*bourses*) and the professional accounting situation (Belgian *Experts-Comptables* and *Revisors*). This chapter concludes with an interesting digression on the development of *Accounting Plans*.

In the following chapter, the Accounting Law of July 1975 which remains the core of the new accounting legislation in Belgium is tackled. After indicating what enterprises are subject to this Act, the author illustrates the fundamental principles underlying the Act, and the exceptions for small enterprises as mentioned in art. 5 of the Act. Turning to the different articles involved in the basic law of 1975, he briefly discusses: vouching, annual accounts, records and books, form and contents, consolidated accounts, smaller firms (exemptions of art. 12), implementation, the *Accounting Standards Commission,* derogations and exclusions and the law's enforcement.

Chapter 4 subsequently deals with the Royal Decree on Annual Accounts of October 1976 implementing the basic law of 1975. The most important articles are discussed together with the Ministers' Report to the King, before turning to some differences between this Royal Decree and the Fourth Directive of the E.E.C. The role of the *Centrale des Bilans* as a depository and dispatching center of annual accounts is then emphasized. This chapter elaborates further on some principles of accounting in which leasing, the overall fiscal influence in reflecting true and fair values in the accounts, together with revaluation and inflation accounting are considered. The author concludes with the illustration of the role the Belgian *Accounting Standards Commission* can play in interpreting accounting principles.

Although consolidation was not settled within the previous accounting legislation, a special Royal Decree was issued in November 1977 dealing with consolidation for holding companies. This topic is discussed in Chapter 5, showing the failure to consolidate group accounts with the example of the largest Belgian holding company, *Société Générale de Belgique*.

Chapter 6 reopens the discussion on the Uniform Systems of Accounts. As mentioned in the Law of 1975 and the Royal Decree of 1976, a *Minimum Normalized Chart of Accounts* had to be elaborated and was finally imposed through a new Royal Decree of March 7, 1978. Forrester emphasizes also in this chapter the importance of commitment accounting together with claims and counter-claims. He concludes this chapter discussing the C.I.G.E.C. (Centre d'Information de Gestion des Experts Comptable), pointing out that data processing exchanges between France and Belgium were facilitated "by the use of compatible Plans Comptables in each country" (p. IV/42).

Management accounting aspects are briefly summarized in Chapter 7. Forrester concludes this *Issue No. 4* with the following assertion: "In aspiration over decades, and now feasibly, Belgian accounts fulfil both capitalist and socialist purposes, and inform private and public decisions. If for this reason alone, the intent, the wording and the effects of recent Belgian accounting legislation is worth attention" (p. IV/44). *Issue No. 4* ends with a postscript on holding companies, some bibliography and annexes showing pre-reform published information, a model balance sheet and Profit & Loss account under the 1976 Act and the Chart of Accounts of 1978.

Issue No. 4 contains a tremendous amount of precious information on the Belgian case in developing accounting legislation, so that the reader who takes a quick glance at it might well be favourably impressed. We also do agree with Professor J. P. Gillet in his foreword to *Issue No. 4* that "Writing such a comprehensive and understandable article on the new Belgian accounting legislation is no small achievement and the author deserves congratulations." This performance is even more impressive if we consider that the author is a foreigner.

Nevertheless, a more profound investigation reveals a number of weaknesses, errors, and shortcomings. One of the major difficulties of the author in tackling this topic will certainly have been the language problem. When scrutinizing his bibliography, for example, no Dutch articles are quoted.

The Dutch literature, however, would have revealed another approach in the discussion on annual accounts and the increased demand for information. The French approach traditionally inclines to more emphasis on the registration regulations, as where a Dutch approach emphasizes more *disclosure* requirements. This controversy led to the adoption of the first Draft of a Fourth Directive as the basis for further discussion on implementing a new accounting legislation in Belgium. The difference in emphasis can best be illustrated when taking into account another prior aspect of the total renovation in information disclosure requirements in Belgium, i.e. the Royal Decree of November 27, 1973 providing financial and economic information to the Industrial Relations Councils. It is really a pity that Forrester excluded this Royal Decree from the scope of his analysis because in it the main emphasis was placed on *disclosure* rather than on *registration* requirements. "The requirements of the types of reliable information that should be released (disclosed) are indeed more important than are the requirements of how the accounting data must be processed. In this regard, we can refer to the etymological sense of the words, where "enregister" means to put into registers (input—*opsluiten* van informatie) and "disclosure" has just the opposite meaning, that is to release information (output—*ontsluiten* van informatie)."[1] In the same context, it must be observed that a great many terminology problems emerged in the translation of the French texts into the Dutch version, due to the fact that preliminary drafts were in most cases originally drawn up in French and translated into Dutch afterwards. So, for example, the French text is dealing with "*avoirs*" which implies all "assets" of the firm, while the Dutch counterpart incorrectly translates "*avoirs*" as "*tegoeden*" which means "*receivables.*"[2] Forrester, however, only notes that "Laws and decrees are of course drafted and enacted both in French and Flemish," (p. IV/17) not considering the terminological problems in the sense mentioned above (p. IV/19-20). Belgium has a problem like that of the E.E.C. in general. Namely an accounting standard in one language must be almost totally rewritten for another language. In all E.E.C. legislation, the translation from the original working text to the member languages is not a trivial problem, but must be carefully executed by experts in accounting.

As to the discussion on the role of the Public Auditors in Belgium, Forrester did not mention an important Recommendation to the Government by the National Economic Council of July 12, 1972.

As to the auditing profession in Belgium, three major problem areas might be discerned:

a) accounting standard setting does not exactly imply that auditors will meet the standards, leading to a performance gap. Furthermore an expectations gap will occur due to the fact that public expectations of the work performed by the auditors might differ from the standards set by the profession.
b) the profession is confronted with a vicious circle of low fees, low scope, low quality, low image and low fees.
c) the problems arising from an audit monopoly situation in Belgium, where only a very restricted number of public auditors can legally and officially perform the audit required for firms quoted on the Stock Exchange.

After several drafts, a Royal Decree dealing with Public Auditors might at last appear in 1983.

The introduction of a Minimum Normalized Chart of Accounts in Belgium (p. IV/37-42) was also a strongly debated topic, although the organizations of accountants and revisors (public auditors) favoured such a Royal Decree on Uniform Systems of Accounts. The discussion centered around advantages and disadvantages of Uniform Charts of Accounts. The merits of Uniform Systems of Accounts, however, should be measured by criteria, such as:

a) information criteria: defining *what kind of information* the accounting system should be able to provide.
b) control criteria: the accounting system should be able to provide *reliable information*.
c) economic criteria: reliable information should be processed in *economically acceptable conditions*, in a *labor-saving* way.

Turning to the discussion on E.D.P. processing, Forrester refers to "such modern data processing methods" (p. IV/29. In reality there exists a very large gap between the accounting practices and the text of the new accounting legislation. Art. 8 of the Law of 1975 emphasizes mainly the importance of books, which must be "certified, numbered and initialled" (p. IV/20), leaving some possibilities open to "replace them by alternative measures guaranteeing the regularity, completeness and continuity of matter in the books" (p. IV/21). Nothing much, however, has been realized in this matter up till now. In this way, art. 8 is introducing a modern anachronism into a body of new accounting legislation.

As to the company financial data deposited and dispatched on computer tapes through the special Agency of the Central Bank of

Belgium (*Balansen centrale—Centrale des Bilans*), recent studies of Jegers and Buijink have demonstrated that registered annual accounts do not meet the necessary criteria of reliability. So for 1980, for example, they conclude that less than seven percent of the annual accounts are reported correctly.[3] Omissions and arithmatic errors are numerous and are not merely due to transcription inaccuracy.

About the *Tableaux de financement* or Funds Flow Statements (p. IV/25) Forrester argues that the "government anticipated that the law would eventually require" (p. IV/25) such statements. If he had been working through some preliminary working texts or drafts, he might have discovered that Funds Flow Statements were required, but that in later drafts this topic was finally dropped and given as a general consideration in the Report to the King. In light of this opposition, it might still take many years before Funds Flow Statements, however defined, might be accepted in new accounting legislation.

Also the Belgian legislators have been inconsistent in dealing with inflation accounting. No alternative methods are imposed on Belgian companies to show the effects of inflation on annual accounts, except for replacement costing and revaluations. This differs from the Fourth Directive. It is too strong an assertion to say that "replacement cost accounting . . . is forbidden except as auxiliary calculation and report in the decree" (p. IV/28), because firms are allowed to use this method.

If many firms do not use replacement cost accounting it is merely due to the fact that this system is not acceptable for the Belgian Tax Authorities. Furthermore, Forrester is wrong in arguing that "base stock methods for inventory valuation" (p. IV/31) are allowed in Belgium.

The author of *Issue No. 4* stresses the deficiencies in the Profit and Loss account (p. IV/25) only based on the nature of costs. He omits in his analysis to mention the difference between the Royal Decree of 1976 and the Fourth Directive on this matter (p. IV/27-28). The Fourth Directive allows also for a Profit and Loss account presented on the basis of cost allocation. The Belgian Royal Decree does not, suggesting that the Belgian legislators still have to discover modern analytical cost accounting methods. This might also help to explain why in the Minimum Normalized Chart of Accounts classes 8 and 9 are left free and undefined, and could of course be used especially for Cost Accounts. (Appendix IV, see also p. IV/40)

It is furthermore somewhat surprising to see that Forrester wants to present a current picture of the Belgian economic environment *anno* 1980 (publication date) when on several occasions he refers to statistical data which were already ten or more years old. For example, data on "Companies registered at local Commercial Courts" goes back to 1970 (p. IV/8), Cobbaut's study on dividend policies of 1969 covers the period 1946-1965 (p. IV/10) etc. . . . At least the author should have updated his empirical evidence in the text.

Finally, I believe *Issue No. 4* deserved a better editing. Photoprinting from a typewritten copy sometimes results in an illegible presentation. This is especially true in the Appendixes.

Although *Issue No. 4* contains several faults and shortcomings it remains a valuable piece of research and provides the nonspecialist and non-Belgian a concise and comprehensive overview of the topic. In this regard, it would be appropriate for classroom discussion.

FOOTNOTES

[1]Lefebvre, p. 114.
[2]Lefebvre, p. 115.
[3]Jegers and Buijink.

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Arundel Cotter, *Fool's Profits* (New York: Barron's, 1940. Reprint edition, New York: Arno Press, 1980, pp. ix, 174, $16.00).

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Fool's Profits is a series of articles that were originally published in *Barron's* during the period, August through November, 1939, plus three appendixes containing sections of government documents relating to the acceptability of LIFO for income tax purposes. Cotter indicated, "this volume is not written primarily for the accountant, but rather to the corporate executive, particularly those concerned with finances, and directors as well as students of corporate finance and business generally" (vii). The book represents a crusade by Cotter to get corporations to adopt LIFO rather than FIFO.

Cotter's advocacy of LIFO arises primarily from the belief that it will result in smoothing income. He has no real concern for balance sheet valuation of inventory. His approach to this advocacy is to provide examples of the effects on profits of industries and companies within industries over periods of five to twenty years. In addition, he provides, as examples of how smoothing is obtained, some simple numerical computations. Peculiarly, he is so enthused about LIFO that he continually refers to it as "inventory control."

The book might have had considerable impact at the time of its publication and it might have been an important book at that time; however, it is not a book that I would recommend be high on one's reading list. I found the costs of reading the book far exceeded any insight into accounting thought at that particular time and accounting thought during the second quarter of the twentieth century is a subject in which I am interested. Perhaps, one of the reasons for my negative attitude towards this book is that I recently read Devine's book on accounting for inventories [1942]. The Devine book which was published about the same time as *Fool's Profits* was written for accountants and, even though it is somewhat boring at times, it provides a great deal of insight into the origins of LIFO and accounting thought of the period.

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