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The Field of Management Services As Seen By The CPA

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WHAT is a real profession? The best answer to this question that I have heard was given by the Executive Director of the American Institute, Mr. John L. Carey. He listed the characteristics of a profession as "*Technical Competence* in a field of knowledge requiring advanced intellectual training; the use of *judgment*; the acceptance of *responsibility*, the assumption of *authority* in its own field; a sense of *mission*, a desire to help people, a willingness to share their worries, to aid their hard decisions."

Each of these characteristics is important, and no one can be stressed over the other. A *sense of mission* and the *use of judgment* certainly are not sufficient without *technical competence*.

A professional man must be an educated man. A description that appealed to me appeared in *Fortune Magazine* in an article by Russell Kirk. He said:

A person truly educated in the humane tradition should have an orderly and disciplined mind—so far as any system of training can bring order into private personality. He has been taught the relationship between cause and effect. He should understand that predictable consequences follow from particular actions. He has in his mind a fund of precedent. He is acquainted with system. He has been taught a respect for just authority, and that the ego must be kept in check. The complexities of modern business require precisely those habits of thought that a liberal education has been trying to inculcate in young men these several centuries.

Business is concerned with just one thing—making a profit. Of course it is true that a business not run to satisfy the wants of its customers, one that is mismanaged or dishonest, will die. But the reason for its death, finally, will be lack of profit—thus no capital. And making profit is a very high motive—one that has carried our standing of living above that of all other nations of the world, although our start was below the standard enjoyed by many countries when our country was founded. Profit is the reason lying back of our terrific progress in health and welfare, the great drug companies and world-renowned doctors and surgeons having their origins in this country.

A NATURAL FIELD FOR THE CPA

The emergence of accountancy as a profession has its basis in one thing: service; service to the public, which includes as one of its principal functions assistance to business in making this profit. Now it is true that much of our time is consumed in preparing reports regularly required by law for various purposes, which reports may or may not have a bearing on the making of profits. Many certified public accountants are so busy with routine services for clients that the nearest they come to management service is to concentrate to some degree on tax problems, which may save money for the taxpayer but is not a profit-making *management service*.

Advisory Management Service is a *natural* to CPAs. In fact, I know of no profession whose members have a more intimate knowledge of a client's financial condition and of the detailed operations of his business than the accountant. Only the individual himself, or management, would have a comparable understanding.

Are we spending so much of our abilities on less important functions that we are losing sight of the fundamental reasons for our services? Our work falls far short of fulfillment if it is limited to preparing a tax return or delivering an audit report when we have capabilities far beyond that point. It was interesting to note from a statement in a report of the International Congress of Accounting held last summer in Holland that management consulting work by professional accountants is making much more headway in the United States than in other countries.

These services present both a challenge and an opportunity: the challenge of a broader field and scope of work, and an opportunity to offer a variety of services to clients.

BROAD BASIS OF EXPERIENCE

The accountant cannot, and will not, disclose confidential information. However, within ethical limits, there is no reason why he cannot recommend for one business the successful general business methods he has learned during his wide experience. Nor is there generally any reason why he cannot place in operation, and then supervise, such methods in another client's business activities. I am speaking, for instance, of such things as forming inventory committees, expense committees, or car-pool control, but not of competitive information peculiar to a certain business or industry. For instance, the general information acquired in practice, that money can be gotten at 4 per cent rather than the 5 per cent a particular client might be paying,

is usable, but obviously it cannot be disclosed that a certain client might have a special 4 per cent arrangement with a certain source. Care must be taken to utilize only facts that can be generally considered common knowledge and therefore available if one is alert, in contrast with specialized, confidential or semi-confidential information.

OBJECTIVITY

Management is understandably grateful to those who help achieve greater financial success for their companies, and the opportunities for certified public accountants to give such assistance are much greater than is usually recognized. Because of the very nature of their work, they can often achieve a more objective picture of a company's operations than can management itself. They can bring a fresh approach to both old and new problems—to those affecting the financing and financial operation of a company as well as to those of a general nature.

THE CPA'S IMPLEMENTS OF SERVICE

What I am sure you want is the answer to this question—What specifically can we, as the accountants, do to accomplish the desired results for the client, namely, greater efficiency of operations and a better profit return?

In our firm we have a department called *Management Advisory Services*, which is staffed with competent systems men, trained as accountants and industrial engineers. They perform a necessary and valuable function for the business public. I am not a member of that department, however, and that is not the type of management service I shall discuss today.

I do not minimize the impact of electronics on accounting. It appears that we are in the early stages of an accounting and business management revolution, which in some respects will rival the industrial revolution in its effect on the lives of everyone. The revolution in office procedures and data processing promises to do for man's mind what the industrial revolution did for his body.

I recommend for your reading an article appearing in the *Accounting Review* for April, 1958, entitled *The Impact of Automation on the Field of Accounting*, a paper presented by C. L. Keenoy, Vice President of National Cash Register Company. This article brings home to the accountant, better than anything I have read, the fact that "a trip to the moon by rocket" can affect even *your* clients. Every practitioner should have some knowledge of electronic application to office procedures. I quote Mr. Keenoy:

Accounting is facing the most challenging, yet potentially rewarding era in its history. By "challenging" I mean that today, as never before, the accountant must remain abreast of every major development in data processing. By "potentially rewarding" I refer to the profession's golden *opportunity* to offer *ever-broadening* services to management.

Important as this is, I do not feel qualified to give a paper on *Electronic Data Processing*. I am most interested in the individual accountant, whether his firm be large or small, who is constantly alert to help business management in all those ways in which an accountant should be most proficient.

EXPERIENCE AND JUDGMENT

A case in point is an experience we have had with a small warehouse business. For several years we furnished this client with informative audit reports. To us the reports showed a most unfavorable trend in the business, but the management was completely "sales minded" and had no interest in either discussing or reading the general recommendations furnished with our reports. The sudden death of the President, and other circumstances, accelerated the trend we had observed. Even an untrained financial mind could see that their usual loan commitment was not adequate. When we discussed this with the surviving management, they showed obvious interest in anything that would rectify the continuing drop in the bank account. After talking with the banking institution concerned and the company's major suppliers it became obvious that serious long-term planning was necessary. The company first got rid of an "ingrown" Board, at our suggestion, and the Board of Directors was reorganized with an attorney and a prominent business man, not connected otherwise with the company, replacing company employees on the Board. Regular meetings were held (which had not been done in the past), usually at our office and with us participating, although not on the Board. A cash-flow forecast was prepared, based on carefully thought-out sales forecasts and collection charts and trends. A young man was hired who is capably taking over the monthly forecast revisions and analysis of differences between forecast and performance. With our help this young man has installed a system for keeping the inventory balanced and for planned purchasing. Together with the client we conferred with suppliers and credit grantors to cement relations with suppliers and obtain extended credit lines both from suppliers and from banks, thus enabling the firm almost to double its inventory.

Still, it should be underscored that none of these engagements ever end with the heroine and hero living happily together forever after, all of the dragons slain, never to rise again. This firm has its face set in the right direction. Meetings of the Board of Directors are serious work sessions and are regularly held. There are no "yes men." At a recent meeting, for instance, the new President announced he had made arrangements to handle a certain item that many of their customers used, which could be sold without any investment in inventory; that although it was a low-profit item (gross profit being 7 per cent as compared with about 20 per cent on their regular items) it would not cost anything to stock and the whole 7 per cent would therefore be "gravy." His young assistant did not agree, stating that as the regular overhead was about 15 per cent of sales he felt they were losing money by handling the item. Discussion by the Board pointed up that the thinking of both had elements of truth and elements of falsity—that the overhead would be substantially the same *in dollars* whether or not they handled the item. However, the principal danger we pointed out was that they were short of working capital, and borrowed money cost them 7 per cent. Therefore, sale of such a short-profit item would have to be held strictly to thirty-day term. For them to carry a \$100 account representing a \$7 gross profit for ninety days would cost them about \$1.80; with the salesman's commission and proper bad-debt provision deducted, profit would be practically eliminated. Sales of this item are a service to the customer and probably result in other warehouse sales; however, all agreed the situation should be closely watched.

There are so many instances where an accountant can be of great help to the business man. Management advice, budgeting, and financial planning extend into virtually all phases of every type of business. Not surprisingly, in snowballing fashion, this extension creates more work for the accounting firm and for the profession, but not at increased cost to the client. Generally the result is increased profits for the business.

INTEREST AND TECHNICAL COMPETENCE

We must always remember that the measure of success of our work is the benefit flowing to the client because of services we have rendered. By enthusiastic interest and watchful attitude, the accountant can often find opportunities to aid a client at the most unexpected times.

For instance, a client called to say he had found a "good buy" in a piece of property that was going into escrow that afternoon and

wanted to let the auditor know how his attorney had advised holding title. The accountant, being thoroughly familiar with this client's affairs, was disturbed that the man might be purchasing an "expensive bargain." If the client kept the property, rentals received would not pay out the property because of his income tax bracket. On the other hand if he sold it at a capital gain, he would only aggravate an already burdensome estate problem.

The solution proposed by the accountant, and immediately adopted by the client, was to create a trust. A comparatively small gift was made to the trust; the trust purchased the property subject to a trust deed to be paid off out of income from rent, taxed at substantially lower brackets than the individual income tax of the client. The trust is paying off the loan from net rents and accumulating a nice estate for the beneficiary, which will not be diminished by estate taxes on the death of the creator.

Such opportunities for service can only be recognized if the accountant is always vigorously searching for new areas in which he can be useful, and if he has over a period of time become thoroughly conversant with the affairs of his client.

REQUISITES FOR THE ADVISORY FUNCTION

Let me warn you again that a sense of mission alone—the desire to help—without technical competence and use of judgment can be a dangerous thing. Some of us have heard a young junior on a new audit assignment reporting excitedly how the client is doing everything wrong—and some things worse. He has to be told there was a good reason underlying each practice—and perhaps a very complex reason. Technical competence comes through education and experience.

The use of judgment in the management field also comes primarily through experience.

Accounting firms that have not equipped themselves to render expanded services may face the loss of clients who want more than audit and tax work. A member of the American Institute's Council, Mr. Michael Bachrach, in an article in *The Journal of Accountancy* for March, 1958, suggests that the problem can be solved by a plan of cooperation and referral between smaller practitioners and larger firms with management-services departments.

It has also been my feeling that some experience in the private field—in bookkeeping, stock-room control, shipping, or other branches of private pursuits—is valuable background for a young man who plans to enter the public accounting profession. I say it is *valuable*

background; I do not say it is *essential* background. Some of the finest accountants I know, men who are alert and experienced in the management field, went into public accounting straight from the classroom, and gained their management experience through observation and by maintaining an inquiring mind. Such a course recalls the adage about education: A man does not have to go to school to get an education, although going to school makes it easier for him to become educated.

Judgment in the management field requires an evaluation of people. A system, method, or procedure that fits one client beautifully may not be at all suitable for another in substantially the same circumstances. The explanation lies in the differences between people in the two firms who will carry out the recommended proposal. Enthusiastic cooperation from the manager on down the line is necessary for smooth functioning of new methods and procedures. And I am also referring to top management, because methods that would appeal to a *sales-minded* management may need to be modified to obtain the same results for a *production-minded* management.

THE ART OF COMMUNICATION

This brings up another point of the subject, which to my mind warrants serious consideration by accountants.

Each ten years or so there seems to be a single word that becomes popular and is used by about everyone under almost any circumstances. In the present era, with its marvels of telephone, radio, and television, the word is *communication*, and top executives in these fields are being called *communicators*. We hear complaints on all sides about the difficulty of communication, no matter how wonderful the means available, and accountants have been criticized time and again for their lack of proficiency in this important part of their work. One of the most outspoken critics was the late Mr. C. F. Braun, President of the Braun Company, and engineer and author. In his book *Objective Accounting*, he said: *The training of the average accountant binds him to narrow arithmetical conceptions and makes him quite unequal to the dynamic realities and needs of modern industry. It can be fairly said that industrial accountants as a whole have done the world's worst job of communication*

While in my opinion he has grossly overstated the situation, this criticism of our power of expression has been made so often by business men, and by accountants themselves, that we must admit it has a basis in fact. Of what use is a well prepared financial statement, bud-

get, or cash forecast if the management does not read and understand it? Of what use is a well thought-out plan for improving your client's operations and increasing his profits if we cannot get him interested in it?

To my mind, the place to begin is the audit report, accounting statement, or other financial information we are asked to prepare. These are most effective when personally presented by the accountant. Meet with the executive committee, the general manager, or whoever is going to use the statement. Discuss it with them and answer their questions regarding it. By so doing you are not only educating them in what an accounting statement means and what its purposes are but, if you stay alert, you are learning their fields of interest and their problems and at what points in their operations your experience might be most useful to them.

It is particularly desirable to discuss the financial statements with the management and their bankers. When the banker joins with the management and the auditor in a close review of the financial statements, the management becomes more sharply aware of what benefit the auditor and the financial statement can be to him.

Accounting statements can be made understandable to anyone of intelligence who is interested. You may have seen the article by Stuart Chase written for *The Lamp*, a publication of Standard Oil Company of New Jersey, and reprinted in *Texas Magazine* for May, 1958, entitled *How to Read an Annual Report*. Here is a CPA who knows how to communicate. He lists ten basic questions that should be answered in each report and in clear, simple language explains the principal financial statements. Time does not permit a discussion of this article, but we can all benefit from reading it.

ESSENTIALS FOR PROGRESS IN THE FIELD

As an accountant I am proud of my profession. We have made great strides in establishing generally accepted principles and in improving our abilities and service. But let us not allow the complexities of modern business or the importance of proper auditing and tax planning to blind us to the existence of broader constructive fields for our services. Our minds have been analytically trained and we should make the best use of that training.

A word of caution: Our services are *advisory*. The impression should never be given that we are trying to run a business. A sense of mission for the accountant in the management field means a sin-

cere desire to help his client, to share his client's worries, to aid the client in his hard decisions, but not to make those decisions.

In conclusion, then, an accountant as advisor on management and financial planning is not very different from the same accountant preparing an audit report, a tax return, or a budget and cash forecast. He needs those reports as tools, but that is only the beginning of his rôle as advisor. Much work and no little exercise of judgment lie ahead.

Our experience, and the experience of other accountants with whom I have talked, has been that financial planning and management services are not always separate engagements. They flow naturally from an accounting or auditing engagement. But this will only occur when that service—and may I again use John Carey's words—is rendered with. . . *evidence of a desire to help, to relieve the client of care, to take responsibility. . . . Professional men not only work, they worry. They don't just lay reports or opinions on the client's desk. They share with him the difficult tasks of forming judgments and making decisions.*

An alert management will change the very cornerstone of its operation if by so doing there is a real opportunity to increase profits. The prosperity of a company and the prosperity of our country depend largely on ability to change with the changing times and on willingness continually to make improvements. In the challenging years ahead, this will be even more true than in the past. The need for certified public accountants to participate in this continual progress is urgent and immediate.

In assuming these broader responsibilities the accountant will find in his work the deep and abiding satisfactions without which any profession has scant purpose and meaning.