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Retrospective: Paul Franklin Grady

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RETROSPECTIVE:
PAUL FRANKLIN GRADY

Abstract: This paper, written by his son-in-law of 37 years, is a collection of anecdotal "folklore" about a man who had a very significant impact on the development of the accounting profession during the "Golden Age of Accounting". Paul Grady's greatness arose from his enormous dedication, strength and character, coupled with his complete honesty and relentless ruthlessness in seeking to have his views prevail.

The only purpose in the paper is to provide a glimpse of the nature of this truly remarkable person. If the paper fails in this, then perhaps the reader will at least find the stories mildly amusing.

Paul Franklin Peterson (sic) was born in a log cabin in Creal Springs, Illinois on May 19, 1900. He was born prematurely, weighing less than three pounds at birth, and was not expected to survive. Family tradition has it that, at birth, Paul was wrapped in a blanket and placed in a shoebox surrounded by heated bricks from the cabin fireplace. The heat from the bricks provided warmth and Paul did make it through that first night. Perhaps this was the initial indication of a fighting spirit and a will to overcome difficult situations that seems to characterize many highly successful persons of his era.

When Paul was five, his father, James Peterson, developed tuberculosis and, for reason of the elder Peterson's health, the family was compelled to move to Colorado in 1905. Later that year, James Peterson died and Paul, his mother and younger brother, Merrill, returned to southern Illinois, settling in the town of Marion. More than fifty years later, Paul first learned, as a result of an X-ray examination in connection with an application for life insurance, that he had, at an early age, also been the victim of tuberculosis. Apparently, although the trip had failed to cure the elder Peterson, Paul's undiagnosed case of the lung disease was unknowingly cured.

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On the return trip from Colorado, Paul's mother, Myrtle Powless Peterson, met J. J. Grady, whom she subsequently married. At the time of her second marriage, however, Paul's name was not changed to Grady; he made the change himself upon reaching the age of eighteen. His brother, Merrill Peterson, never changed his name.

While growing up in Marion, Paul was a good student, excelling in mathematics and the physical sciences. This latter was important in that there was a substantial amount of coal mining locally and Paul developed an interest in mining at an early age. This prompted him to apply to the University of Illinois in 1918, seeking a degree in Chemical Engineering. We may speculate that this early interest in science and geology created a common interest with Herbert Hoover, who later became not only Grady's close personal friend but also his idol. Further, this close association with Hoover is in part, at least, responsible for Paul's continuing support of the Republican party and his strong conservative positions on many issues throughout his life.

Two additional aspects of Paul Grady's high school years; one is that, even though he was a short man, he excelled in basketball, being captain of the Marion high school team. From this experience, we can see again that element of Paul's character that caused him to succeed, even though he was not physically well suited, in one of the few major sports in town at the time.

The second aspect of Paul's high school years was his love of Louese Trevor, a local beauty who was a cheerleader for Marion High. She also had a lovely singing voice. Paul and Louese planned to be married after his graduation from the University of Illinois, anticipated in 1922. In the meanwhile, Louese went to Chicago Music College for three years after high school, to further her interest in music.

In the later years of his life, Paul said "I've only been in three partnerships in my life; one with Arthur Andersen, one with Price Waterhouse and one with Louese Trevor." Of the three, the latter was clearly the most lasting; Paul and Louese remained married for sixty two years, until Paul's death in 1984.

Once at the University of Illinois, Paul found that there was not time enough to take the demanding physical science courses, with afternoon lab sections as well as morning lectures, and to hold down a full time job, which was necessary to sup-
port himself, his family back in Marion and to provide savings for his anticipated marriage. After his third year, Paul was forced to abandon his chosen work in Chemical Engineering, in order to have the afternoons available for work, leaving evenings for study. [In all the years that I knew Paul, I never heard him express disappointment at not completing his major in Chemical Engineering, but I suspect that it must have been a difficult choice for him to make.]

This allowed Paul to take a full time job, working afternoons and early evenings as a short order cook at Ostrand's, a family run delicatessen serving the college students of Champaign/Urbana. This arrangement worked well and, in fact, after two years, Mr. Ostrand offered a partnership share in the restaurant, an offer which Grady considered and rejected. He did, in later years, speculate on the implications of this decision on the course of his later life; I get the impression that he enjoyed being a short-order cook and often reminisced about the prospects of a quiet life catering to students at Urbana.

One further aspect of Paul's experience at Illinois was the beginning of his lifelong friendship with Andrew Barr, who later became Chief Accountant at the Securities and Exchange Commission.

Another lifelong friendship was with Ralph Johns, who was later associated with General Motors. The University became the beneficiary of this relationship in the early 1960's, when Paul served as Director of Research for the American Institute of Certified Public Accountant. The story goes that John Carey, then Executive Director of the Institute, called Paul upon the occasion of Paul's retirement from Price Waterhouse in 1960, offering the position of Director of Research of AICPA, which was vacant at the time. Paul, reluctant to take the offer at all, finally agreed to take the job for a period of one year only, spending the time writing Accounting Research Study No. 7, "Inventory of Generally Accepted Accounting Principles". Carey agreed to these terms and informed Paul that the annual salary for the position was $125,000. Paul replied that he did not want the salary, but Carey insisted that the position would pay that amount of compensation, whether Paul wanted it or not. Paul called his friend Ralph Johns, saying that he had $125,000 to "give to the University of Illinois, if you (Johns) would match the gift". Johns agreed and this money became the seminal contribution for the Center for Studies in International Accounting at the University of Illinois.
Upon graduation from the University of Illinois, Grady took a position with the relatively new firm of Arthur Andersen & Co., Chicago. He also passed (barely) the CPA exam in the state of Illinois. Regarding his experience with the CPA exam, he related to me that, when he had completed taking the exam, he went to his room to wash up and dress for dinner. While washing his face, he realized that he had not answered one of the questions on the exam, a cost accounting question for a coal mining operation. He said that he had read the question early in the exam session and had put the question aside to be solved later, because he felt very confident that he could answer the question easily, having previously worked as cost accountant for a coal mine. He then devoted a majority of the allotted time to what he considered to be the more challenging questions, completed his answers to these and turned in his work. Fortunately, his work on these other questions was of sufficient quality to garner a passing grade on the exam without the answer to the coal mining question; certainly, learning that he passed was a substantial relief to Paul. I believe that the foregoing story is the only known incidence of any admitted error by Paul Grady, at least to my knowledge.

While at Arthur Andersen in Chicago, Paul's career advanced rapidly. He traveled some in the early years and Louese traveled with him. He tells one story of spending a week in a small town in central Illinois, auditing the local bank. All during the week, both he and Louese noticed that the townspeople were avoiding them for some reason; they even crossed the street to avoid meeting them on the same sidewalk when they were out for an evening stroll. Finally, toward the end of the week, Paul inquired of the lady who ran the boarding house where they took their meals concerning the attitude of the townspeople. Her reply was that the people were very suspicious of "those strangers, particularly that fellow who sits all day at a desk in the front window of the bank, making those funny looking marks with a bunch of different colored pencils."

As Paul's career with Arthur Andersen proceeded, Arthur, Sr. placed more and more reliance in Paul's ability to get the job done. Paul was asked to go to New York in 1931, to help open a New York office for the firm. Paul did this and remained in New York until 1937, when he returned to the Chicago office.

At one point in the late 1930's, Arthur, Sr. took a trip of several months to Europe. During Arthur's absence, one of Grady's chores was to write an Audit Manual for the staff of the
firm. The task was completed and the manual was distributed to the staff prior to Arthur's return from Europe. Upon his return, Arthur reviewed the new document and objected strongly to the emphasis in the manual placed upon review of and reliance on the client's system of internal control. Apparently, Arthur believed in the more traditional balance sheet approach to auditing and withdrew the manual from circulation within the firm. This difference of opinion was one of many between Grady and Andersen and may have contributed to their eventual parting of the ways, which occurred in 1945.

For Grady's part, he was very active in the early development of the American Institute of (Certified Public) Accountants and worked to get the notion of reliance on the system of internal control adopted by the Committee on Auditing Procedure; an effort in which he was largely successful. He was fully in favor of the definition of internal control that prevailed in the accounting literature for some years; namely that internal control was comprised of three facets; *internal check*, which was designed to safeguard assets, *internal accounting controls*, those controls designed to "provide for the reliable and accurate recording of accounting data", and *internal administrative controls*, which were designed to "promote operational efficiency" and "provide for compliance with management's prescribed policies". Further, I know that Grady's personal view was that an auditor should be responsible, under Generally Accepted Auditing Standards, for reviewing all three aspects of internal control, even though a case can be made that *internal administrative controls* are not directly related to the reliability and accuracy of financial statements. He justified this belief by saying that the auditor is qualified and able to render services to audit clients beyond the narrow scope of what is required to reach an informed opinion on financial statements. While others of the time disagreed with Grady on this point, I feel that this view is the precursor of the now well recognized position of the profession in rendering a host of services to clients, beyond the normal audit service.

During the Second World War, Grady was asked by Secretary of the Navy James Forrestal to come to Washington to review and revise the Navy's Procurement and Cost System, a job which Grady considered to be his patriotic duty in time of war. He remained in Washington until 1945, when his work was completed and the War was drawing to a close. He indicated that, during the latter stages of the war, Arthur, Sr. had con-
tacted him regarding returning to Chicago to resume his position as an active partner in the firm's growing practice. Grady refused to do so, on grounds that the national interest in time of war required that he complete his work for the Navy Department. This disagreement with Arthur, Sr. perhaps was the last straw in a series of disagreements; at any rate, Arthur, Sr. asked Grady to either return to Chicago or resign his partnership. Grady, understanding that his partnership agreement with the firm contained a noncompeting clause for a period of ten years from his resignation, refused to resign. The disagreement finally became so serious that Arthur, Sr. agreed to fire Grady, thus making it possible for him to accept a partnership with another firm. Thus, after completing his assignment in the Navy Department, Grady accepted a partnership in the firm of Price Waterhouse, in the New York office.

I know that the break with the Andersen firm was a very trying time personally for Grady. According to Grady, Arthur, Sr. put a great deal of pressure on the other partners to force Grady's resignation. As a result, most of the partners were afraid to have any social contact with Grady during the final year or so of Grady's tenure with the firm. Both Paul and Louise related one instance where, while attending the theater, one of his partners who was also in the audience was afraid to speak to the Gradys in public, but, instead, covered his hand with his program as he waved his greeting to Paul.

Two other stories come to mind regarding Grady's post-Andersen years. First, I have often heard him express his high regard for James Forrestal and the work that he did at the Navy Department during World War II. Grady did feel, however, that, while the relationship between Forrestal and President Roosevelt was a good one, the same was not true regarding Forrestal's relationship with President Truman. Indeed, Grady expressed the belief that the attitude taken by the new, post-war President towards Forrestal probably contributed to Mr. Forrestal's decision to take his own life shortly after the conclusion of the war. While he did not express the nature of the "bad blood" between the two, I am sure that, in Grady's mind, Truman should have accepted some portion of the blame regarding Forrestal's demise.

The second story was related by Paul Grady to me in late 1983, perhaps early 1984, just months before his death. It seems that the management consulting firm of Booz, Allen, Hamilton was in the process of being formed about the same time that
Grady was considering his offer from Price Waterhouse. Apparently, Grady was approached by Booz (and/or perhaps Hamilton), asking him to accept a partnership in the new management consulting venture, the new firm to be called Booz, Grady and Hamilton. I know that Grady considered the offer seriously, but rejected it in favor of the Price Waterhouse option because “he felt a little afraid to take on the risks of a new venture (ie., the management consulting business) and preferred to stay in a professional environment where he felt comfortable”. In retrospect, Grady expressed to me that “while he certainly could not fault his relationship with Price Waterhouse, I wonder how things would have turned out had I chosen to go into the consulting business.”

On technical issues, there are several stories that he told that were, in my view, revealing. One has to do with how Accelerated Depreciation came to be a generally accepted accounting principle. According to Grady, the accounting profession was very interested in the changes taking place in the tax law in 1954, when Congress passed the Internal Revenue Code of 1954. According to Grady, he and other representatives of the AICPA who were working with members of the Congress on the legislation, felt strongly that the new tax law should reflect the impact of rising prices on the American taxpayer by giving a tax deduction for loss of purchasing power on money invested in securities of corporations when inflation occurred. The Committee would not agree to put this provision into the new law, so the accountants sought a compromise that allowed a deduction to corporations that had significant investments in fixed assets during times of inflation. The compromise was to allow faster than straight-line write-off of plant and equipment for tax purposes. Once accelerated methods of depreciation were acceptable for tax purposes, it only required a short time for these methods to become GAAP, presumably in order to reduce the number of book/tax differences that would otherwise be created.

While Grady did not necessarily agree with the methodology of FASB Statement No. 33 (he did not believe, for instance, that companies should recognize gains or losses on net monetary asset/liability positions), he did agree in general that companies needed some ability to reflect the impact of inflation financial statements. He also felt, I believe, that, once we instituted a rational method of accounting for inflation, we should probably not continue to allow Lifo and Accelerated Deprecia-
tion to be used concurrently.

Another story told by Grady deals with the history of accounting for deferred income tax. During the late 1940's and early 1950's, a substantial debate occurred over the issue of "clean vs. dirty surplus"; in other words, should all items that were not properly associated with the balance sheet be components of income? The "clean surplus" proponents believed that there were no such things as proper debits or credits to earned surplus (retained earnings); that all such items were elements of current net income, even though they were extraordinary or nonrecurring. The "dirty surplus" proponents held that income should be a measure of the recurring, usual earning capacity of the enterprise; therefore items of an unusual, nonrecurring nature should be taken directly to Stockholders' Equity ("Earned Surplus").

Sometime in 1983, Paul remarked "You know that Mr. May (George O. May) would have a fit if he realized what he started regarding all this deferred tax business ... Some years ago, he wrote an article (I think in the Journal of Accountancy, but I'm not sure) on the clean/dirty surplus argument saying that he 'really didn't want to comment on the clean/dirty surplus argument but would urge that, whatever is decided as regards that issue, we should include a rule to require that, if an item is to be included in income, the related tax effect should also be included in income and, conversely, if a item is to go directly to earned surplus, then the related tax effect of that item should not be allowed to remain in income.' [Parentheses mine.] Grady felt that this was indeed a simple idea that made plenty of good sense; he was simply amazed that that simple idea, according to Grady, was the beginnings of the entire deferred tax problem.

Although he never discussed the matter with me, I seem to remember reading in a history of Price Waterhouse that Grady had inferred in a personal interview with the historian that he had not been elected to the Executive Committee of that firm because he joined the firm late in his career, rather than "coming up through the ranks". The historian went on to suggest that, despite this, he was indeed a very powerful partner in the firm; further, the historian suggested that he maintained his position within the firm by never being argued down or proven wrong on any technical accounting or auditing point.

Indeed, within his family, Paul never, to my knowledge, admitted error (with the exception of the story, told above, about leaving out the mining cost accounting question on the CPA
exam). Family folklore in this regard includes the story that his wife, Louese, told, that "Paul has only made one mistake in his entire life. In 1951, he thought he had made a mistake but it later turned out that he didn't!!"

This "bulldog tenacity" was exhibited by Grady even after his retirement from Price Waterhouse at age 60. Paul spent eighteen months (roughly 1961 and half of 1962) completing Accounting Research Study No. 7, "Inventory of Generally Accepted Accounting Principles", then he and Louese moved from their home in Greenwich, Connecticut to Delray Beach, Florida. Upon establishing residence in Florida, Grady sought a reciprocal CPA certificate from the Florida Board of Certified Public Accountants but his application was rejected, along with that of his friend Percival F. Brundage, who was seeking reciprocity in Florida at the same time. Grady reported, in a rather indignant manner, that the Board had rejected his application because of lack of academic credit for a Freshman English course in Composition (Grady had "tested out" of the Freshman English requirement at the University of Illinois, so his transcript indeed did not show that he had taken the course). Further, Grady said that "Percy got rejected because his BA degree was not from a properly accredited university". (Brundage's undergraduate degree was apparently from Harvard University.)

This turn of events clearly did not suit Grady, but I did not hear much about the matter until, a year or two later, Paul announced that he was now a member of the Florida Board. It was also about this time in Florida's history when that state's "Blind Tiger" rule finally fell and large firms were allowed to practice in that state under their own names. I have no way of knowing if the two events (Paul's success in becoming certified in the State of Florida and the demise of the "Blind Tiger" rule) are related, but I have always somehow suspected that they almost simultaneous occurrence was somehow not coincidental. I do know, however, that Paul was eventually successful in his application for certification by reciprocity; I am not aware of the outcome of Mr. Brundage's application.

In summary, I now believe that the primary characteristic of Paul Grady's personality is this tenacity in pursuing those things that he believed were right, coupled with very thorough analysis of every situation to insure that he was right. (Indeed, family folklore aside, he really was almost never wrong, at least when it came to technical matters. This was the benchmark of his professional reputation.) Perhaps his classmates in the Se-
nior Class of 1918 at Marion Township High School came to appreciate this characteristic early in Paul's life. The quote which the editor of the school yearbook chose for Paul's Senior Class picture is "A decent boldness ever meets with friends." [The Memory Kit].

WORKS CITED

The Memory Kit, annual yearbook of the Class of 1918, Marion Township, Marion, IL.