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CPAs investigate financial reporting

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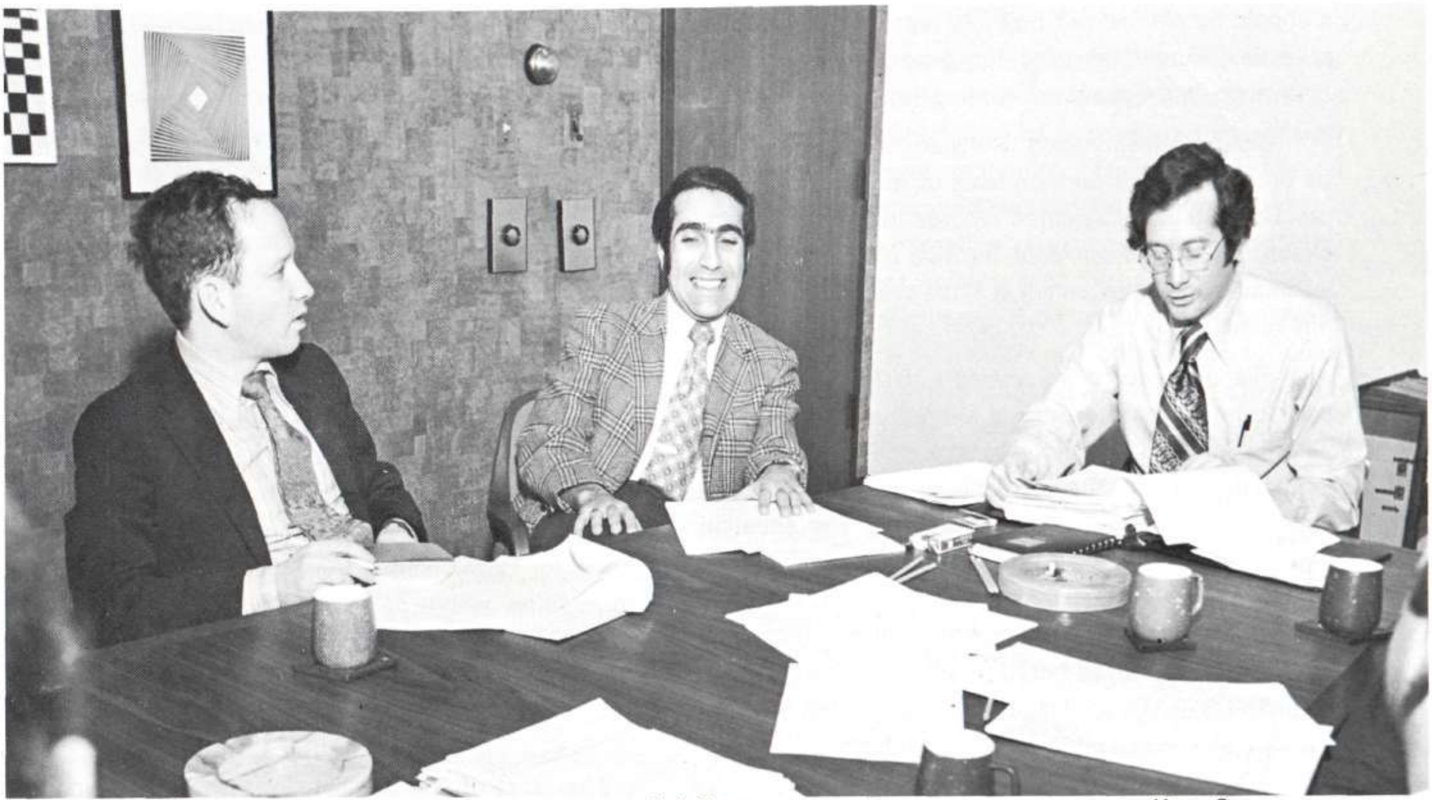
CPAs INVESTIGATE FINANCIAL REPORTING



Paul Rosenfield — Josh Ronen — Marty Gans

Public Hearings—Dates & Places

Chicago
April 17 and 18, 1972
Palmer House

New York
May 15 and 16, 1972
Americana Hotel

Accounting Objectives Study Group

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There has long been an uneasy feeling that financial statements do not tell all they should and that we have no clear idea what they should tell. Every accountant has seen financial statements that are camouflaged to hide accounting trails as convoluted as a mess of worms. Today—when business is being judged by its effects upon the environment and upon people—should the financial statement disclose these effects?

Many questions about financial reporting were raised with publication of the Accounting Principles Board's Statement No. 4, *Basic Concepts and Accounting Principles Underlying Financial Statements of Business Enterprises*. The objectives stated—relevance, understandability, verifiability, neutrality, timeliness, comparability, completeness—are rather abstract, and are limited to current procedures. They give little consideration to expanding needs or to how financial reporting might be improved to cope with those needs.

With the purpose of studying and refining the objectives of financial statements, the Accounting Objectives Study Group was formed early in 1971 by Marshall S. Armstrong, then president of the American Institute of CPAs. Chairman of the Study Group is Robert M. Trueblood, who is also chairman of the Touche Ross Board of Directors and our National Director of Accounting and Auditing.

Trueblood defines the problem

Trueblood defines the problem as follows: "What we need, but so far have been unable to develop, is a statement of basic objectives that allows the structuring, the identification, and the analysis of potential problems and solutions—a statement of basic objectives responsive and relevant to the needs of users. *This* is the objective of our Study Group."

Under Trueblood's direction the Accounting Objectives Study Group reviewed the literature of accounting, financial analysis, economics, and the behavioral sciences without finding many explicit data on accounting objectives. They decided they would have to discover the answers themselves and consult with people who *use* financial statements.

The Study Group has nine members—from academia, the profession, and the financial community. It has a full-time staff of six, with the same broad range of backgrounds. Staff coordinator is Marty Gans, a manager in the Executive Office of Touche Ross in Chicago.

A questionnaire is being used as a springboard for interviews lasting two hours or more with a cross section of business leaders and decision makers. Each of the interviewees receives, well before the interview, a guide to identify the issues and to raise questions in his mind. Each interview is conducted jointly by at least one Study Group member, together with a member of the staff.

What the Group wants to know

What they want to know, in general, is: (1) How is accounting information used? (2) What additional information is considered necessary or desirable? (3) Is furnishing such information feasible?

Flying much higher, they urge respondents to consider and talk about the importance of accounting in: (1) allocation of resources, (2) planning national growth, and (3) providing a setting of accountability to aid in controlling the economic system.

The questionnaire is broken down into six divisions. In the first, called "analysis of the decision process," the respondent is asked what financial decisions he makes and how often—not only for his business, but also for his civic, social and other responsibilities. Information is elicited concerning what data are used for these decisions, how they are obtained and evaluated, and what other data would be desirable.

Under "the role of accounting information in making decisions," decisions on lending money and buying or selling investments are probed for the influence of traditional data such as risk, yield, ratios, and financial statements—as against data on product lines, backlog, intangible resources, competitive position, and predictions of future income, dividends, GNP, strikes, and cash flow.

The heading "economic events to be described by accounting" includes questions on whether financial reports should tell about such items as product development, development of human resources, market fluctuations, technological changes, wage-price freezes, pollution, conservation, and goal setting.

"Measurement of events" is the heading for questions about whether the present valuation base is logical. It might be more precise, for example, to evaluate inventory as $240,000 plus or minus 10%—or to use replacement prices, exit prices, selling prices, or discounted cash values.

The next section investigates the "extent of detail, order and emphasis in accounting reports," with questions on whether fixed and variable costs should be separated in the income statement, whether assets should be grouped by relative risk of realization, or whether consolidated reports should be replaced by separate reports on each product line or division or corporation. Respondents are asked whether the order and form of financial-statement captions and footnotes should be standardized.

Finally, under "attestation of accounting reports," respondents are asked if attestation forms might be revised, particularly on proposed new types of reporting, without diminishing their value.

Public hearings

Public hearings have been scheduled by the Accounting Objectives Study Group so that all significant segments of opinion on these questions can be heard. In view of the sharp divisions among the financial disciplines and others about what should or should not be added to financial statements, or changed in them, these hearings should provoke fireworks.

Over 4,500 organizations and individuals were formally invited to send in position papers to the Study Group. Among these were all companies listed on the New York and American Stock Exchanges, state CPA societies, over 50 governmental, business and professional groups, 100 international accounting organizations, 100 AICPA member firms, and scores of universities.

The Study Group hopes to digest these masses of opinion and information in time to report significant achievements next autumn at the annual meeting of the AICPA.

Change is essential

Change is essential with changing times. As Bob Trueblood has said of the Group's challenging assignment: "Identifying objectives consistent only with the status quo reduces motivation for change, however deficient or however unsatisfactory the present may be. Such myopia inhibits the orderly evolution and growth of the profession. And when orderly evolution and growth are inhibited, revolution too often follows."