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CPA and his profession

Maurice H. Stans
Arthur B. Foye
John L. Carey

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The CPA and His Profession
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The Profession of Accounting

BY MAURICE H. STANS, CPA
Chairman, American Institute of Accountants committee on CPA Handbook

PART I: PUBLIC ACCOUNTING, PAST AND FUTURE

The growth of the profession of public accounting is one of the outstanding phenomena of the Twentieth Century!

In the United States, this growth has been especially pronounced. Following slow gains in the early years after 1900, the number of those engaged in the profession began to increase rapidly around the time of World War I at a rate which has accelerated with each succeeding decade. In the ten years from 1940 to 1950 the number of public accountants approximately doubled — with a numerical increase much greater than the gains in the older professions of law and medicine, and in the newer engineering and scientific professions.

Even more striking than the expansion in number of practitioners is the continued broadening of the scope and influence of public accounting. It has evolved from a mere policing operation to a constructive social force.

By its contributions to the advancement of the economic processes, the profession is repaying its obligation to the industrial revolution which gave it birth and early impetus. As an independent medium in economic relationships, it is becoming an important factor in the movement toward social understanding. By a simple projection of the past into the future, it stands on the threshold of vaster opportunity.

History of the Profession

The great American philosopher, Ralph Waldo Emerson, once wrote that "the use of history is to give value to the present hour and its duty." The history of the accounting profession, from its genesis to the present time, gives outstanding proof of the soundness of this proposition. In this history, the fact of great growth, while impressive, is of much less
significance than an understanding of the forces that gave the profession momentum and brought it to its present size and stature.

Prior to 1900

The history of the profession of independent public accounting prior to 1900 is sketchy and sparse. The name of the first public accountant is undoubtedly lost forever, but he probably was an able bookkeeper, employed by an early Italian venturer of the Fifteenth or Sixteenth Century, who achieved such a reputation for technical skill in his work as to be consulted by others for advice in handling their records of transactions. In terms of the art of accounting as it then existed he was a person skilled in accounts and, when he made himself available to more than one employer, he became a public accountant. The earliest recognition of financial record-keeping as a specialized occupation occurred in Venice in 1581, when the first College of Accountants was organized. An applicant was required to serve a 6-year apprenticeship with a practicing accountant and pass an examination. Thereafter, he became an “expert accountant,” but since businesses were small and mostly owner-managed his functions were principally in the field of bookkeeping assistance.

In those days, therefore, public accounting was little more than public bookkeeping. No doubt there were occasions, perhaps many of them, when partners in the spice trades or in silk importing disagreed among themselves over their shares of profits, or creditors disagreed with debtors over amounts due, and an independent person with skill and experience in accounts was called in to learn the facts and render a decision. Their names, too, are lost to history, and literature gives them little recognition.**

* The earliest written work on bookkeeping, which set the stage for public development of the accounting art, was the Italian “Account Keeping” by Lucca da Borgo Pacioli, published in 1494.

** A. C. Littleton, in his scholarly work, “Accounting Evolution to 1900,” discloses the names of one of the first public accountants in England from an epitaph, taken from a slab in the chancel of St. Mary’s Church, Chesham, Buckinghamshire: “Here lyeth part of Richard Bowle, who faithfully served diverse great lords as auditor on earth, but also prepared himself to give up his account to the Lord in heaven . . . He died on 16th December 1626, and of his age, 77.” Littleton points out that except for the auditing of municipal and government accounts as early as the Fourteenth Century by selected local members of the public, who could scarcely be called public accountants, there was no record of any public auditing by experts until the practice arose, probably early in the Seventeenth Century, by the lords of the large manor estates, of employing specialists such as Bowle to check their accounts. When the center of economic life began to shift from the agricultural manors to the towns with the beginnings of manufacturing, the earliest signs of a recognized public profession emerged. The city directory of Edinburgh, for the first time of any in the British Isles, in 1773 listed seven persons as accountants serving the public. At the beginning of the Nineteenth Century less than fifty public accountants were recorded in the directories of all of the large cities of England and Scotland.
Nevertheless, it is clear from the brief notes that history provides that public accounting can trace its origin back to the early days of trade and commerce. But, in comparison with the law and other established professions, it was wholly insignificant until the development of the industrial revolution and, in particular, the institution of the "limited company" or private corporation, first in England and later in this country. The greater capital and size of these expanding entities naturally caused more accounting problems to develop, but the real need for an independent accounting group sprang from the fact that absentee investors, now an important and growing class, came to want impartial and unbiased reports from time to time on the safety of their investments and the outcomes of their ventures.

When British capital came to the United States in the latter half of the Nineteenth Century, public accountants followed, and the profession in this country originated with a definite English and Scottish stimulus. Many of the early American railroads and utilities were thus financed and the investments thus watched. In time the profession was augmented by the creation of new firms in this country, as the opportunities grew and the number of practitioners enlarged.

1900 to Date

Despite the many years since its birth, the public accounting profession by the year 1900 was (in terms of subsequent growth, at least) still in infancy. In the United States there were only 243 individuals who had achieved the right to call themselves certified public accountants under recently enacted state laws. Of these, ninety-two had become members of a professional organization, the American Association of Public Accountants (predecessor of the American Institute of Accountants). The entire profession of public accounting, including noncertified practitioners, staff members and clerical employees, in all probability numbered little more than 1,000 persons. Their services consisted largely of the independent auditing of the accounts of large corporations, although they also undertook some work of installing accounting systems. Emphasis was principally on the mathematical aspects of accounting rather than on its broad character and potential uses.

In the succeeding fifty-two years the profession has grown spectacularly. The table here shows the numbers of certified public accountants in the United States at the end of each decade:

<table>
<thead>
<tr>
<th>Year</th>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>1900</td>
<td>243</td>
</tr>
<tr>
<td>1910</td>
<td>1,712</td>
</tr>
<tr>
<td>1920</td>
<td>4,997</td>
</tr>
<tr>
<td>1930</td>
<td>13,560</td>
</tr>
<tr>
<td>1940</td>
<td>20,169</td>
</tr>
<tr>
<td>1950</td>
<td>38,104</td>
</tr>
</tbody>
</table>
In 1952 the total passed 45,000, pointing toward a probable 60,000 certified public accountants in this country by 1960.

But these figures tell only part of the story of the profession’s gains. To the current count of certified public accountants must be added a vast group of licensed and unlicensed public accountants. And to measure the real size of the profession, it is necessary to include the thousands more who make their living within it—staff members, trainees, clerical and office workers, stenographers and typists.

From a 1950 survey of the United States Department of Labor¹ come these estimates:

*Individuals (1951)*

<table>
<thead>
<tr>
<th>Category</th>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individuals, engaged professionally in public accounting</td>
<td>90,000</td>
</tr>
<tr>
<td>Professionally trained accountants in private accounting work</td>
<td>150,000</td>
</tr>
<tr>
<td>Total of all professional accountants (including those in industry, government and all other activities)</td>
<td>300,000*</td>
</tr>
</tbody>
</table>

*Accounting Practices (1947)*

<table>
<thead>
<tr>
<th>Category</th>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sole practitioners</td>
<td>19,000</td>
</tr>
<tr>
<td>Partnerships (including 11,000 partners)</td>
<td>4,400</td>
</tr>
</tbody>
</table>

*¹ From 1900 to 1950, while the population of the United States doubled, the total number of lawyers increased from 115,000 to about 190,000 and the total number of doctors from 132,000 to about 180,000.

If the latter figures as to practices were brought up to 1952, they would probably turn out to be at least 24,000 partners and 5,500 partnerships, respectively. If the estimate of 90,000 professional accountants in public practice is expanded to include nonprofessional employees, the total number of individuals engaged in public accounting probably becomes nearly 150,000.

**Significance of Growth**

There must be fundamental significance to an expansion of such extent and rapidity in the demands upon a new profession. What forces account for its spectacular expansion in the space of a little more than half a century until its size has increased to one hundred and fifty times its proportions in 1900? Has society merely found it necessary to introduce a new type of police force to help regiment and discipline its economic activities? Is this development merely the addition of more and more sleuths and checkers to keep trial balances in balance, scare cashiers into honesty, and detect peculations by bookkeepers? Many laymen still believe so. It is unfortunate but true that the expansion in size of the profession, when recognized at all by those outside it, is usually associated

¹ See references at end of this chapter.
with ideas such as these. The expansion in scope of the profession’s functions, and the extent of its contributions to business progress in the last fifty years, are not well recognized by the general public, to whom public accounting means auditing and auditing means a policing operation.

It is not surprising either that, under the pressures of increased calls for their services, most accountants have little time to take stock of the importance of their own actions to the profession and the place of the profession in the broad scheme of things. The day-to-day work and decisions are the trees so numerous that they obscure the forest. It is all too natural for one with a growing clientele to concentrate on his own financial progress, and to pay but token respect to the position and standing of the profession of which he is a part, and with which his own present stature and future prospects are closely tied.

Figure 1. Growth of Public Accounting Profession in the United States
(Number of Certified Public Accountants Only)
The individual public accountant can serve his clients better if he has a broad concept of the importance of his profession, its obligations and its opportunities and — in simpler terms — how it fits into the workings of the whole of society. If he understands his professional responsibilities, his social responsibilities, his ethical obligations and his legal obligations, he will be a better accountant and, with advantages to him and to his profession, a better citizen.

**Influences for Growth**

In broad terms, economic forces have developed the profession at such a rapid pace because the last half century has been a dynamic period. Since 1900 the forces unleashed by the industrial and social revolutions

![Figure 2. Membership in the American Institute of Accountants, Including its Predecessor](image-url)
have brought the profession to its present standing—and these same forces provide the challenge which it faces in the years ahead.

In order to appraise the future more fully, some specification of these growth influences is necessary. With an enumeration and evaluation of the individual forces that have cumulated their demands upon the profession in the last fifty years, the future course is more predictable. In this analysis, the development of the art of accounting and the development of the profession of public accounting are sometimes indistinguishable, because the relationship of cause and effect frequently shifts position between them.

Demands on Accounting

In broadest terms, three highly significant trends have brought about the increased importance of accounting since 1900:

1. The great expansion of industrial activity, based largely upon the products of scientific research, with widespread ownership of large corporate enterprises and with greater demands on accounting for financial control.
2. The increase of government influence in the affairs of business, especially through taxation and regulation.
3. The search for increased productivity in industry, through the development of mass production systems, with their great emphasis on cost control and efficiency.

In viewing these trends, Percival Brundage² spells out the important "milestones on the path of accounting" during the last fifty years as follows:

"1. The consolidations and mergers of the early years of the century with their effect on accounting;
2. The beginning of government regulation of accounting in 1907;
3. The growth of accounting with high taxation during World War I and the beginning of the shift of emphasis from the balance sheet to the income statement;
4. Adoption by the New York Stock Exchange of standards of accounting disclosure in 1932, further developed by the Securities Acts;
5. Emphasis on accounting during World War II— in research bulletins, in price fixing, and in cost inspection, repricing and renegotiation;
6. Postwar developments in accounting, particularly those due to inflation and enhancement of the position of organized labor and the farmer."

His following summation of the place of accounting in this period is eloquent:

"During the 50 years of the Twentieth Century...the developments of business and of accounting have been great and have reacted upon each other. Without the aid of accounting machines, improved methods of internal control, and adequate reporting, large-scale operations by business would have been impossible. The economies of mass buying and distribution through chain outlets might never have been realized. The statement, frequently heard, that 'accounting is a tool of business' is true, but not the whole truth. Accounting is also a partner of business.”
Professional Contributions

The ways in which the profession held up its end of the partnership by meeting the challenges of these milestones were many and complex. They are part of an impressive history too long to be detailed here. They include the growth and geographical expansion of some of the early accounting firms; participation in the development of a working structure for the tax laws; the organization and combination of professional organizations into the present American Institute of Accountants; the evolution of a professional literature, of standards of examination and qualification, and educational curricula; the institution of research committees to deal with accounting principles, auditing standards, terminology, disclosure and other technical areas; co-operation (to the same end) with the stock exchanges, the Securities and Exchange Commission, and other public and governmental bodies; assistance to the government in budgetary matters, in wartime accounting problems and in many other fields; the training and graduation of several hundred thousand skilled accountants for the ranks of industry and government; and aid to industry in meeting the innumerable problems of expansion, taxation, regulation, financing, creditor and stockholder relationships, cost control, operating efficiency and profit making.

It is a history of which every accountant-participant can be proud, because it helped to build the most productive industrial system the world has ever known. This could not have been accomplished by business without the teamwork of accounting, private and public.

The result in stature of the accounting profession is told in this quotation from an official government publication:

"Accounting is an indispensable tool of modern business organization and management. Professionally trained accountants (numbering about 800,000 in 1951) set up the accounting systems which make it possible for even the largest corporation to record, classify and summarize its myriad daily financial transactions. They also analyze and interpret business records and prepare reports showing companies' financial standing and the profit or loss on past operations. Financial statements prepared by accountants enable business men to plan future activities in the light of past experience. Investors frequently rely on accountants' reports in deciding to buy or sell the stocks and bonds of particular companies. Banks use them as a guide in approving or rejecting applications for loans. Public service commissions find these reports essential in approving or disapproving requests for rate increases from telephone, gas and electric, and bus and streetcar companies. Even the smallest business firms need financial statements prepared in accordance with professional accounting standards in order to compute taxes owed to the Federal, state and local governments." ¹

But this is not the ultimate. There are more milestones ahead, even though their shapes are not yet clear. The widening road leads into a long and distant horizon, far beyond view. In such a circumstance, the varying problems ahead can best be met by the generation of a fundamental philosophy, founded on an objective of creative usefulness and geared to the needs of a dynamic economy under democratic processes.
**What Is Public Accounting?**

**Definitions**

One place to seek for a philosophy for public accounting is in its definitions. These definitions take their roots, of course, in definitions of accounting itself. The well-known English philosopher, John Locke, once said, in a different context, that “accounting is a business of reason, not of arithmetick.” A committee of the American Institute of Accountants has described accounting as “the art of recording, classifying and summarizing in a significant manner and in terms of money, transactions and events which are, in part at least, of a financial character, and interpreting the results thereof.” One of the general dictionaries defines it merely as “the art or science of keeping accounts.” In more eloquent terms, one writer called accounting “that elegant discipline.” To the accountant, the more significant of all these expressions are those that characterize accounting as a process of reasoning or interpretation, for it is these qualities that lift his work above the level of the mechanical.

With the addition of the qualifying adjective “public,” to define an area of service and also a profession, there are added to accounting two connotations—one of service to a general clientele, the other of responsibility to the public interest. It is the second of these that is least understood.

**Public Impressions**

Edward B. Wilcox once defined the certified public accountant as “the guardian of the conscience of the business community.” This expression, and others of similar vein sometimes heard, are correct as partial characterizations, as was intended in the context employed, but they do not reflect the whole area of service or of responsibility. They lean too heavily on the early function of the accountant as a verifier, and correspond too much with the layman’s conception of public accounting, which has lagged far behind its actual development. To too many of the public, the public accountant is the auditor of Elbert Hubbard:

“The typical auditor is a man past middle age, spare, wrinkled, intelligent, cold, passive, noncommittal, with eyes like a codfish, polite in contact, but at the same time unresponsive, calm and damnedly composed as a concrete post or a plaster of paris cast; a human petrifcation with a heart of feldspar and without charm of the friendly germ, minus bowels, passion or a sense of humor. Happily, they never reproduce and all of them finally go to Hell.”

Too many members of the public, too, have heard and remembered the indicting voices of certain labor leaders, leveling accusations like this one:

“Many of the financial statements being issued are really understatements of income accounts. This practice must cease . . . .”

As a result of these kinds of shenanigans . . . income accounts have come to be not true representations of profits and income. They have been referred
to by some labor economists as subtle interpretive summaries. Many of our people have come to completely mistrust most of the published accounts of corporations. . . ." 4

Addressed as they were to accountants, these remarks carried the implication that accountants, and public accountants in particular, were responsible for the alleged misrepresentations. These and many similar statements and implications are almost wholly unfair and unrealistic, and in some cases they undoubtedly spring from ignorance or from deliberate fiction, but they point up the facts that (1) a single ill-conceived action by one public accountant can bring damage to the entire profession and (2) professional consciousness of responsibility and professional organization are necessary to establish and maintain the certified public accountant’s reputation for integrity and independence.

**Need for a Philosophy**

**Individual Attitudes**

In too many instances individual members have seen the profession grow up without recognizing its organized achievements and without participating in them. A casual attitude toward organized research projects, a rugged resistance toward their conclusions and a smug satisfaction at individual success conspire frequently in the accountant’s philosophy to cause him to overlook the fact that his is not an individual effort but a participation in a profession. The unfortunate result is that some practitioners lag, in philosophy, far behind the professional organizations that are trying to lead them. They fail to grasp the primary fact that the evolution of public accounting is part of a revolution in economic and social thinking — a revolution which accounts for the profession’s growth in the past half century and particularly in the last twenty years.

No one individual can pretend to know or to put together all the relationships in this complex civilization in which public accounting is so important. Yet it requires little more than a single quotation like this to recall the origin, the purpose and the end objective of the accounting process:

"Great economic and social forces flow with a tidal sweep over communities that are only half conscious of that which is befalling them. Wise statesmen are those who foresee what time is thus bringing, and endeavor to shape institutions and to mold men’s thought and purpose in accordance with the change that is silently surrounding them." 5

To this need be added only one sentence: Accounting is the principal means of measuring economic relationships. Since accounting is the language of business, it is the best means of conveying public understanding of the economic facts of life.
**The Real Objective of Accounting**

A subtle test of the public accountant's function in the workings of the broad economy is to ask for a definition of the work of a doctor or an engineer. Is a doctor merely a man who administers pills and cuts out infection? Is an engineer merely one who builds bridges and designs tools? Or is a doctor a part of a learned profession that is continuously seeking to extend the life and health of man? And is an engineer a member of an educated profession that is aiming to advance the physical comfort, convenience and safety of man? The analogy should be clear. Is an accountant merely one who writes debits and credits and checks trial balances, or is he in the important sense a member of a skilled profession the ultimate objective of which is to accumulate and interpret the facts that measure the contributions and rewards of the various groups that make up our industrial-commercial society?

Recognition of this distinction is all that is necessary for the accounting practitioner, large or small, to recognize that he is an important cog on a big wheel in the socially powerful economic machine.

**Responsibilities and Obligations**

The public accountant, in his capacity as a professional man, assumes the responsibilities and obligations general to all professions. He also undertakes certain social, ethical and legal obligations arising specifically from the unique character of his work and its relationships to the public.

It is generally understood that three elements must be present before a man's activities can be called professional:

1. Special knowledge and appropriate skill.
3. Recognition of an inherent public interest.

These elements of professional standing are in turn the responsibilities of any member of a profession.

**Professional Responsibilities**

An essential obligation of a professional man is that of competence. He must not undertake to offer his services to others generally unless he has reason to believe that — through education, training, experience and personal characteristics — he is able to serve effectively. To undertake an assignment which is "over his head" is as unfair to his profession as it is senseless from a wholly practical standpoint, since the risks of failure are too great.

In the field of auditing especially, the accounting profession has undertaken to spell out the applicable standards of competence. Of course, the same obligation of professional competence that applies in auditing work applies to work undertaken in all other areas of practice, including the handling of income tax matters, accounting system installations, the
broad field of business counselling and all other services.

It is a point so logical that it need not be belabored. To each business operator or other person who seeks out the services of a public accountant, the one he selects is the accounting profession. His impressions of the profession are based on his experiences with his public accountant. In the composite views of all such clients lies the reputation of the profession. The weakest members, unfortunately, weigh heaviest in the balance in the appraisal of a profession, from the mere fact that competence is the essence of the professional function and incompetence is conspicuous.

The other elements of professional responsibility are really subtopics of competence and, like competence, also are ethical obligations. Maintenance of the highest possible quality of workmanship is one. Preservation of the confidences of clients is another. Continuous learning is still another, for failure to keep informed as to changes in the principles or techniques of the profession automatically converts competence into incompetence.

An important element of competence is good judgment. Being well informed as to accounting principles and auditing techniques, for example, does not alone establish the accountant's competence, because it is still necessary for him to exercise judgment in applying them to the facts and in formulating conclusions. To a large extent, the capacity of intelligent judgment is derived from experience.

Finally, one of the important professional responsibilities is participation in the advancement of the profession. It is the responsibility of any profession to seek new and better ways of service, through research, experimentation, development of techniques and similar means. No member can properly remain aloof from such activities by the professional organizations, in the expectation of benefiting from them without effort. As a member, it is his responsibility to assist in organized programs for advancement of the profession's capacity to serve, and to support and adopt the conclusions of such research once they are developed. A passive attitude does not fulfill professional responsibility.

**Ethical Obligations**

The certified public accountant who belongs to the American Institute of Accountants is bound by its code of ethics—the Rules of Professional Conduct.

Rules of ethics and conduct are written into some of the state laws governing the practice of public accounting. Many state societies of certified public accountants, and some organizations of public accountants, have their own codes of ethics. Every practitioner should be familiar, of course, with those to which he is subject.

It is perhaps somewhat unfortunate, and probably characteristic of a young profession, that there is no uniform code of ethics for all who
practice public accounting under a license or title. This may improve in time. All that need be said here is that the rules of ethics are to be viewed as minimum standards to be observed in dealings with fellow practitioners and the public. The real meaning of codes of ethics is found not in their words but in their spirit; in this concept, the entire ethical obligation is expressed, simply and adequately, in the Golden Rule.*

Legal Obligations

The public accountant, in his work, assumes numerous legal responsibilities. Apart from the obligation to comply with licensing and other provisions of state laws governing the practice of accounting, there are many enactments fixing civil and criminal penalties for acts that he might commit in the course of his work. Examples are the penalties under the Federal Securities Acts and under the Internal Revenue Code. No recital of these statutory provisions could possibly be complete, and none should be necessary here.

In addition, the public accountant assumes certain obligations at law to his client, and is charged with others as to third persons.

Social Responsibilities

In one sense, the social responsibilities of the public accountant are the sum of his professional, ethical and legal obligations. They express his duties and responsibilities to his profession, his clients and the public.

But there is another and broader sense, in which responsibility becomes synonymous with opportunity — the opportunity of service in the cause of the advancement of society. The essence of this concept was expressed in the first pronouncement of the Institute's committee on accounting procedure in 1939:

"The committee regards corporation accounting as one phase of the working of the corporate organization of business, which in turn it views as a machinery created by the people in the belief that, broadly speaking, it will serve a useful social purpose. The test of the corporate system and of the special phase of it represented by corporate accounting ultimately lies in the results which are produced. These results must be judged from the standpoint of society as a whole — not from that of any one group of interested parties." 8

Earlier in this chapter, reference was made to the need for a broad philosophy for professional accountants. This quotation supplies its basis. The "tidal sweep" of social and economic change in the last fifty years has built a profession, which in turn has helped to build an outstanding free-enterprise economy with the world's highest standard of living.

* Another expression of this is contained in a quotation from a medical society report: "Any system of ethics . . . that seeks to distribute a profession's services on any other basis than the welfare of humanity invites the loss of that profession's right to survival." Journal of Optometry, February 1947.
Unfortunately, that system (and the democratic structure under which it grew) appears at times to be in jeopardy. Two circumstances bring recurring threats to its permanence—the violent class struggles for greater shares in the productive output, and the irregularities and uncertainties of the boom-and-depression cycles.

The "economic illiteracy" of the public has been deplored by many writers as the underlying cause of the labor-capital-management controversies. One corporate executive expressed the problem in these words:

"It is the responsibility of the corporate system to undertake on its own account and to aid others to develop sound economic thought.

The conditions of every new period, especially one which has seen so much change as the last century and a quarter, are strange and unfamiliar. But changes in old theories, developed to explain the new conditions, must be based not on assumptions but on solid facts, if they are to have any value and not lead us into harmful actions. In the development of modern, sound, economic thought, industry and business might well take more initiative.

The corporation has a responsibility to study the present-day economic situations of which it is both an effect and a cause, to cooperate with others in this task, and to make economic truth as widely known as possible." 7

If this analysis is correct, the dissemination of economic understanding and of economic truth is the means of insuring the preservation of American progress. Accounting is in a leading position to help in creating understanding of the system's workings and advantages because of the knowledge of the economic processes which its members possess. The profession has a unique capacity to help in improving the means of communication of business facts in order to create a better understanding of business operations; in developing improved methods of measuring and increasing productivity in order to build a bigger economic "pie"; and in providing facts to substitute for emotion in differences over the division of the economic "pie."

This is true because, as pointed out earlier in this chapter, accounting is so important a means of measuring the flow and the effects of economic forces and economic relationships. In the hands of its experts, accounting can well become an even more important means of creating understanding, confidence and rationality in economic affairs. In this prospect lies the real hope of eliminating the recurring dangers to the permanence of the American system.

This is an imposing proposition and a long-range one. Much has been said and written about it8,9,10 and more consideration is needed. The important thing at this point is that this tremendous area for service be recognized by the public accounting profession as a social responsibility—and as an opportunity.

The Future

It would be wholly unreasonable to expect that the powerful influences that have caused the building of a great profession should suddenly
diminish, for mankind has never retreated from its objective of abundant living. It would be absurd, too, to expect that an imminent achievement of a philosophical Utopia will bring man's individual satisfactions and ethics to the point where he no longer sought accountability from others. For many centuries, certainly, accounting will be an essential component of an increasingly complex social system.

The future, then, is evident. Professional accounting will continue to grow in numbers and in responsibilities, and in terms of history the spectacular progress of the last fifty years is merely a brief prelude to that still to come. The ultimate destiny of accounting will be measured by the vision and capacity of its practitioners.

References


The accounting profession came into being because people needed its services. Changing circumstances have altered the needs and broadened the scope and form of the services required, but the profession has kept pace with the increasing demands made upon it and has expanded rapidly. Greater numerical strength has not been the only characteristic of its phenomenal growth, however. A natural complement to this physical expansion has been the development of its professional organizations and literature, for it is only through organization that a profession's needs for self-regulation can be met, and it is only through its literature that the techniques and rules which have been developed for the guidance of its members can be communicated to them. It is the purpose of this chapter to discuss the objectives and activities of the principal associations of accountants and to list some of the books and other publications which constitute the literature of accounting.

AMERICAN INSTITUTE OF ACCOUNTANTS

The American Institute of Accountants, which today stands as the only national organization of certified public accountants, traces its lineage directly to all the leading national professional accounting societies which have existed in this country. The original organization, the American Association of Public Accountants, was founded in 1887, nine years before New York passed the nation's first certified public accountant law. Soon after the passage of the New York law, similar legislation was enacted in Pennsylvania, Maryland and California. As a means of maintaining the standards established by the new laws and of promoting such legislation in other states, the accountants in several states formed societies which, in 1902, were united in the Federation of Societies of Public Accountants in the United States of America. In
1905 the Federation merged with the American Association of Public Accountants. In addition to individual membership, the constitution of the merged organization provided for membership by virtue of membership in a state society.

Because of the difficulty of maintaining a common standard of professional competence or attainment in view of the differing requirements for the CPA certificate in the various states, the Association's constitution was completely revised in 1916 and, in January 1917, the name was changed to the American Institute of Accountants. Membership in the Institute was to be on an individual basis only, and all applicants for membership were to be examined by a newly created Board of Examiners. In the years that followed, the strength, resources and influence of the Institute grew rapidly.

In 1921, however, another national organization, the American Society of Certified Public Accountants, was formed. The Society's founders looked upon its program as complementary to that of the Institute—the former seeking to unite all holders of CPA certificates, whether or not eligible for admission to the Institute, and the latter maintaining independent standards of admission and did not then require possession of the CPA certificate which, because of lack of uniformity in the requirements of the various states, did not have the same significance in different parts of the country. As early as 1924 a movement was started to bring about the consolidation of the Institute and the Society, but it was decided that consolidation at that time was impracticable. In 1936, however, after much discussion by special committees representing both organizations, a merger was effected. Since that year the American Institute has spoken for the entire profession.

During the years which have elapsed since its emergence as the single national association of certified public accountants, the Institute has grown from a small organization, concentrating on a few basic activities, to a large one, concerning itself with any and all problems affecting the professional practice of certified public accountants. The broad scope of the Institute's interests is evidenced by the varied activities in which it engages. Its objectives, as recited in the by-laws, are the following:

1. To unite the accountancy profession in the United States as constituted by the certified public accountants of the several states, territories, possessions and the District of Columbia.
2. To promote and maintain high professional and moral standards within the accountancy profession.
3. To assist in the maintenance of high standards for the certified public accountant certificate.
4. To develop and maintain standards for the examination of candidates for admission.
5. To safeguard the interests of certified public accountants.
6. To advance accounting research.
7. To develop and improve accountancy education.
8. To encourage cordial relations among certified public accountants practicing
in the United States of America and accountants of similar status in the other countries of the world.

The work of the Institute, all of which is directed toward the achievement of these objectives, benefits each of its members in a different manner, depending upon the special problems connected with his practice. However, a general consideration of its activities, grouped according to the objectives at which they are aimed, will help to point out the many valuable ways in which the Institute serves its membership as a whole.

**Unity of Profession**

It is significant that the purpose which is stated first in the Institute's by-laws is "to unite the accountancy profession;" for unless the support of all eligible accountants is enlisted, none of the other objectives can be fully realized. It is particularly important for certified public accountants to join together for mutual advancement and protection. As members of a young and rapidly growing profession, they need a greater public understanding of their functions than they have yet attained and wider recognition of the importance of high standards for the CPA certificate. The Institute's influence in dealing with legislators, other professions, and the general public depends upon the extent to which it can claim to speak for the whole profession. Its rapid growth in recent years furnishes convincing evidence that the individual accountant realizes the value which he derives from his membership. In 1920 the Institute's membership totaled 1,363; by 1940 it had increased to 5,497; and in 1952 it exceeded 20,000. However, the continued expansion of the Institute depends upon the active co-operation of all eligible CPAs. Membership is open to holders of CPA certificates who have had two years of public accounting experience or its equivalent and who are in work related to accounting.

The Institute is achieving its objective of uniting the accounting profession not only by uniting the efforts of its individual members but also by co-ordinating the work of the state societies. Although the Institute exercises no authority of any kind over the policies or activities of the state societies, the existence of both state organizations and the national society makes for a type of unity which could not otherwise be achieved. The state societies are the sources of information and advice which, collected and interpreted in the Institute, accurately reflect a cross-section of professional opinion throughout the nation and permit the profession as a whole to work with maximum effectiveness.

In 1946 a state society service department was organized as a part of the headquarters staff of the Institute. This department provides a means for the exchange of information about the constitutions, dues, and activities of the state societies and disseminates material prepared by the Institute staff for their use. Instead of operating more or less independently to provide special services for the state societies and chapters, the state society service department has become to a considerable extent a connect-
ing link between all of the other Institute departments and the state and local organizations. A monthly state society newsletter provides the officers of state societies and the editors of state society bulletins with a regular channel of information. State society presidents who are members of the Institute serve on Council, its governing body, and in this way keep further informed of Institute policies and activities.

The Institute also works closely with other organizations in the accounting field. It maintains active co-operative relations with the American Accounting Association, the Controllers Institute of America, the National Association of Cost Accountants and The Institute of Internal Auditors.

**Professional Standards**

Early in its history the Institute began actively to develop standards of professional conduct, recognizing that self-discipline is a necessary foundation for public confidence. All members of the Institute subscribe to its Rules of Professional Conduct—rules which they themselves have developed and which they may amend from time to time as changing conditions require.

**High Standards for the CPA Certificate**

Since its founding, the Institute has worked for the establishment of uniform standards for accounting examinations throughout the country, for it recognizes that the prestige of the profession in one state is not independent of its standing in another and that its nationwide prestige depends on the maintenance of high standards in every state. The present plan of co-operation with state boards of accountancy in presenting the uniform certified public accountant examination was first proposed by the Institute in 1917. Today these examinations, which are prepared by the Board of Examiners of the Institute, are used by all of the states, the District of Columbia, Alaska, Hawaii, Puerto Rico and the Virgin Islands. Most of the states avail themselves of the Institute's grading service performed under the direction of the Board of Examiners. In all cases, however, it is the individual state board which makes the final evaluation of a candidate's ability as demonstrated by the examination.

**Safeguarding the Interests of Certified Public Accountants**

Because public opinion may effectively determine the extent of the profession's growth and development, the Institute has for many years carried on programs to inform the public about certified public accountants and their work. The rapid increase in the number of CPAs and their dispersion into smaller communities where no CPA has practiced before have added to the need for these activities. Therefore, the Institute has developed a long-range, national public relations program which designates the audiences the accounting profession desires to reach and gives a
detailed analysis of the central ideas and facts it wants them to know. An organized effort has been undertaken to inform small businessmen of what the CPA is, what his standards are, and what he can do for them. As a part of this program, the Institute provides pamphlets and reprints which can be distributed by state societies or individual members. It has articles published in scores of trade magazines and engages in co-operative activity with trade associations. The Institute furnishes speakers for meetings of many nonaccounting organizations. It presents network radio programs and also prepares transcriptions for presentation on local stations. As a result of all these Institute activities, many small businessmen are learning about the accounting profession and the advantages of good accounting service.

An important part of the Institute's work of safeguarding the interests of certified public accountants is accomplished through its co-operation with outside groups. In the governmental field, it maintains close relations with Federal agencies in order to preserve the standing of CPAs before these agencies, and it represents the profession in opposing any Federal legislation which would tend to limit its opportunities. The committee on relations with the Securities and Exchange Commission confers from time to time with the Commission's accounting staff and presents the profession's views on problems of current interest as well as on any proposed changes in the rules or regulations under the Acts administered by the Commission.

Among the national business and professional groups with which the Institute works are lawyers and bankers. Through long and patient negotiation between members of the Institute and members of the American Bar Association, a statement relating to practice in the field of Federal income taxation was prepared and, in 1951, approved by the governing bodies of both organizations. This statement serves as a guide in resolving such questions of jurisdiction as may arise between the two professions. The combined efforts of the committee on auditing procedure, the research department, and the public relations department have helped to develop among bankers and other credit men a better understanding of the CPA's work. In order to obtain the co-operation of credit grantors in the maintenance of high standards, the Institute arranges joint meetings of accountants and bankers at the community level and prepares articles on the CPA's responsibilities which are published in periodicals directed to bankers. In all of these ways it helps to increase the acceptance by bankers of audited financial statements.

As a means of improving its service to the growing number of smaller firms and individual practitioners represented in its membership, the Institute has in recent years formed an advisory committee of individual practitioners which is made up of members from every part of the nation. The purpose of this committee is to review all of the activities of the Institute, with the object of recommending to Council such
measures as will make the Institute more useful to its members, particularly in the smaller communities.

**To Advance Accounting Research**

In 1939 the work of several of the Institute's technical committees was consolidated in the hands of an enlarged committee on accounting procedure, and a research department was created to work under the direction of this committee. The Institute had two basic objectives in mind when it organized the research department — to contribute to the advancement of accounting and auditing knowledge, and to develop information which would help the individual CPA. The committees on accounting procedure and auditing procedure, with the co-operation of the research department, are continuously working toward the advancement of accounting and auditing knowledge. Their pronouncements constitute a guide for the profession. The Accounting Research Bulletins, which are issued from time to time by the committee on accounting procedure, are recognized as authoritative statements of generally accepted accounting procedure. The statements and case studies of the committee on auditing procedure are designed to improve the standards and techniques of public accounting.

In 1950 a technical information service was organized in the research department of the Institute. Its purpose is to enable individual practitioners and members of smaller firms, whose opportunities for consultation with other informed practitioners are limited, to obtain an outside, competent opinion on problems which arise in their daily work. All written questions which are received are promptly answered through the co-operative effort of the research department and the technical committees.

**To Develop and Improve Accountancy Education**

The Institute has always maintained a keen interest in the development of accounting education at the university level. Its committee on education holds joint meetings with a corresponding committee of the American Accounting Association, a large part of whose membership is composed of teachers of accounting. Special committees also confer from time to time with representatives of colleges and universities regarding their accounting curricula. The Institute sponsors graduate study conferences which are held at various schools throughout the country and are attended by both practicing accountants and educators.

An important development in accountancy education in recent years has resulted from the work of the Institute committee on selection of personnel. Under the auspices of the Institute, a College Accounting Testing Program was developed. The scores made by the students taking these tests are evaluated on the basis of nationwide norms and now are
being used by many employers as an important factor in careful personnel selection and by colleges as a guidance aid.

**Cordial Relations Among Accountants**

Through its annual meeting and the regional meetings which it sponsors, the Institute seeks to foster a widening acquaintance among certified public accountants of different states and different sections of the country. In addition, field trips by the officers and staff of the Institute bring members in all parts of the country into personal contact with representatives of their national organization.

The Institute participates actively in the Inter-American Conference on Accounting and the International Congress on Accounting. In these ways it endeavors to develop and maintain friendly relations with accountants of similar status in other countries so that full co-operation among members of the profession will be possible throughout the world.

All the activities in which the Institute engages, regardless of the fact that they may be directed at different objectives, have one important characteristic in common — they are all a means of strengthening public confidence in the accounting profession as a whole. Each certified public accountant must have public understanding if he is to enjoy the fullest opportunity to maintain professional standards and to render maximum public service. Therefore, the work of the Institute cannot fail to be of real, though perhaps indirect, benefit to each of its members, regardless of the size of his practice.

**STATE SOCIETIES**

The American Institute can act as the listening post and keep the profession informed of current developments; it can help in the formulation of policies on the national level; but the state societies must act on the information and bring about application of the policies in each part of the country.

In 1897, a year after New York passed the nation's first Certified Public Accountant Law, sixteen men met to form The New York State Society of Certified Public Accountants. Similar societies were organized in other states shortly after the passage of CPA laws in those states, and by 1929 each state had its own society. At present over 25,000 certified public accountants are members of state societies.

The objectives of these societies, though applied over different areas, are parallel to those of the Institute, and the work of the national and local organizations is complementary. All of the state societies have as their basic aims the maintenance of high professional and ethical standards, the development of educational and technical services which will assist the members in their day-to-day work, and the protection of the interests of the public and of the members. Most societies have a strict code of ethics which is rigidly enforced.
Although the activities of the various state societies differ to some extent, the following are illustrative of the services which the societies provide. All of the societies' programs of membership services are geared to give members a maximum of practical aid in their work. During the year most of the societies schedule several tax lectures and technical meetings for their chapters. These meetings stimulate the interchange of ideas among members and provide for the discussion of problems of a local nature. The societies' technical committees are continually engaged in research in general as well as in specialized fields. The work of these committees culminates in papers which are read at the meetings, in articles in the societies' official publications, or in special reports. In these ways the benefits of their research are passed on to the entire membership. The technical committees are also available to answer the inquiries of members and to give them advice when needed. In addition to the regularly scheduled local meetings of the state societies, several regional conferences are held each year under the auspices of groups of state societies and with the co-operation of the American Institute.

The national public relations program developed by the Institute has already been mentioned. Because the most important part of public relations work is personal and local, the Institute distributed to the state societies copies of a handbook which outlines the national program and describes the methods to be used in organizing and carrying out state and local programs. One of the important objectives of these programs is the development of ways of improving the practice and status of small firms and individual practitioners. The societies' efforts to inform bankers and credit grantors of the types of service rendered by accountants have met with much success. Some of the societies which provide bankers and credit men with copies of their yearbooks, containing the roster of membership and the code of ethics, report that on several occasions they have received requests for more detailed information about certain of the members listed. Small firms and individual practitioners benefit from this distribution of the societies' yearbooks because often, in the past, only the larger accounting firms were considered for engagements in the absence of information as to the names and qualifications of others in practice.

Although the objectives of the state societies are parallel to those of the American Institute, certain functions can be performed by one group more effectively than by the other. State legislation, for example, is a subject that must be dealt with by state societies and members of the profession in the states in which there is legislative activity. The type of accounting legislation that will effectively serve the profession and the public interest is best determined by those who are fully aware of local problems. However, standards must be national in scope. Uniform legislation and interstate reciprocity are in the interests of the entire profession, and it is through the Institute that the views and experiences of different state societies can be brought together and uniform accountancy
laws recommended.

There are two basic divisions to the task which the state societies must perform in connection with state legislation. First, they must make certain that no bill of interest to accountants escapes the societies' notice, and second, they must present the profession's views on every important bill to all those who may influence the bill's course. Whenever bills affecting accountancy are introduced, the societies must promptly take steps to get their views before the right people. This is a problem primarily of personal contact. To present the profession's position effectively requires direct lines of communication to committees, key legislators, and interested government officials. The state societies have done extensive work in establishing favorable contacts with members of these groups. In order to alert the societies to pending legislation which will affect the profession, the American Institute endeavors to provide them with all available information concerning bills which will be acted on at current sessions of the legislatures before the sessions convene. The Institute distributes to the societies legislative kits which contain suggestions and material for handling legislative problems. In addition, the Institute has on several occasions actively assisted various state societies in opposing undesirable legislation and in encouraging the passage of desirable measures.

Like the activities of the Institute, those of the state societies are a means of increasing the prestige of the accounting profession in the eyes of the public. While all members benefit greatly from the programs of the state societies, individual practitioners and those who practice in small communities derive particular advantage from their membership because of the societies' efforts to explain the status of the certified public accountant and the value of his services to local businessmen who are in need of these services.

OTHER ACCOUNTING ORGANIZATIONS

The American Institute of Accountants, on the national level, and the state societies of certified public accountants, on the local level, are the only organizations composed solely of certified public accountants. However, there are several professional organizations whose members work in closely allied fields and have many interests and problems in common with the practicing CPA. The activities of four of these associations will be described briefly at this point. Such descriptions are not intended to be exhaustive, but are given merely to review for the reader the scope of activity of these organizations and their contributions to the field of accounting.

American Accounting Association

The American Accounting Association is the successor organization to the American Association of University Instructors in Accounting, which
organization was founded in 1916. In its early years the Association's main objective was the stimulation of an interchange of ideas among teachers of accounting. Recognizing that the interests of teachers and practitioners are in many ways closely interrelated, the scope of the Association's objectives was widened in 1935, and the name was changed to the American Accounting Association. The objects of the Association, as stated in its bylaws, are:

1. To encourage and sponsor research in accounting, and to publish or aid in the publication of the results of research.
2. To develop accounting principles and standards, and to seek their endorsement or adoption by business enterprises, public and private accountants, and governmental bodies.
3. To promote studies of accounting as an agency of control of business enterprise and of economic affairs in general.
4. To improve methods of instruction, and to demonstrate the social benefits of a more widespread knowledge of accounting.

Members of the American Accounting Association derive considerable benefit from the Association's activities in sponsoring accounting research. The work of its committee on accounting concepts and standards is concerned with the determination and expression of desirable accounting objectives and principles. The committee's findings are published in the Association's quarterly journal and, from time to time, special studies and research monographs also are issued. In addition, close contacts are maintained with all research projects in the field of accounting and allied subjects.

The American Accounting Association co-operates closely with other professional accounting organizations. Its committees on CPA examinations, internship programs, and selection of personnel, work continually with the corresponding committees of the American Institute of Accountants. In recent years the American Accounting Association has formed committees on co-operation with the Controllers Institute and with The Institute of Internal Auditors. One objective of the Association's closer affiliation with these latter groups is the development of internship opportunities in the industrial field.

There are at present over 4,500 members in the American Accounting Association. Membership is open to accounting teachers, public and private accountants, governmental accountants, and other persons interested in the advancement of accounting. The teachers of accounting have had a large part in building the professional literature which has served to articulate the basic concepts of accounting as a framework for practice. There exists, therefore, a natural community of interest between teachers and practitioners. Anything which leads to a better acquaintance between the two groups, to mutual understanding, and to full and frank discussion of their common problems is of value to the profession. The work of the American Accounting Association assists in accomplishing all of these desirable objectives. Accordingly, member-
ship in the Association and participation in its activities benefit the individual certified public accountant as well as the profession as a whole.

**National Association of Cost Accountants**

The National Association of Cost Accountants is an organization devoted to the study of the problems of industrial accounting. It is not limited to cost accounting as its name might indicate. The Association was organized in Buffalo in 1919 by a group of thirty-seven leading accountants. Its membership has increased rapidly, particularly during World War II and the post-war era, and today it has more than 31,000 members. Local chapters have been organized in more than one hundred principal cities of the United States and in Cuba and Hawaii. In addition, many industrial accountants in nearly fifty foreign countries are members. Membership in the Association is open to anyone who is interested in its objectives which are:

1. To develop a better understanding of the true nature and value of accounting, especially cost accounting, in industry.
2. To study and improve technical methods and to establish sound general principles.
3. To study the relation of the accounting department to the other departments of industry and business and to develop the most effective means of supplying usable information to these departments.
4. To supply to its members information on the most up-to-date methods and to assist them in solving their individual problems.

Each of the Association's chapters has its own funds and conducts its own affairs under general rules of operation established by the National Association in order to insure uniformity. Monthly meetings are held by each chapter at which industrial accounting problems are discussed by members as well as by outstanding speakers from many fields throughout the country. It has always been the practice of the Association to restrict the subjects for all its meetings and discussions to practical problems. Case studies dealing with the accounting methods of specific industries or with accounting procedures in a particular area are presented frequently at chapter meetings. In addition to the regular monthly meetings, many chapters hold one or two special meetings each year to discuss industrial accounting matters of particular current importance. Every year, each chapter also presents one or more series of discussion forum meetings consisting of several sessions on some important phase of industrial accounting. These forums provide an intensive coverage of the subject and stimulate the interchange of experience and viewpoints.

The National Association conducts an International Cost Conference each year. The technical sessions at these conferences have gained a widespread reputation for the high standard of the material presented and the ability and experience of the men who enter into the discussions.
One of the distinguishing characteristics of these sessions is the emphasis which is placed upon actual practice. The Association also sponsors regional conferences in which sectional groups of chapters participate. These conferences are designed to bridge a gap between chapter meetings and the International Conference by providing a means for exchange of ideas among members located in a particular section of the country.

The Association maintains a research staff which studies industrial cost accounting problems and methods under the supervision of a committee on research. This committee of more than thirty members includes leading industrial executives, professional accountants, and educators. The results of the studies made by the research staff are distributed to the members from time to time.

A technical service department, devoted exclusively to the service of members, is maintained at national headquarters. Its files include several hundred uniform cost systems developed by various trade associations. There also is an extensive library of books on industrial accounting. Members of the Association may submit questions to the technical service department which furnishes them with answers prepared by other members who have had experience with the problem involved.

The concepts and practices of cost accounting are undergoing continual change as more complex needs and applications arise. Through its efforts to establish sound general principles and to develop improved technical methods to meet the changing requirements of industry, the National Association of Cost Accountants renders a service to the entire accounting profession.

Controllers Institute of America

The Controllers Institute of America is an organization in which active membership is limited exclusively to executives who perform the duties of a controller as defined by the Institute and who serve companies of sufficient size to qualify. It was established in 1931, and its membership now includes more than 3,800 financial and accounting officers of the leading business concerns. In addition to the class of active members, there is a class of associate members which is open only by invitation of the Board of Directors to educators, writers and others in the field of controllership and in related fields. Local chapters of the Controllers Institute have been established in more than forty cities of the United States and in Canada and Puerto Rico. The Institute's principal objectives are to develop a progressive concept of controllership, adequate to meet the requirements of modern business, to educate business management and the public in understanding this concept, and to assist the controller in giving it full expression in his own organization.

The Controllers Institute provides its members with a medium through which they may receive and exchange ideas in the field of business man-
agement. Each local chapter or "control" holds regularly scheduled monthly meetings. In addition to these individual chapter meetings, there are four regional Spring conferences and an annual meeting of the entire organization. An important feature of this annual meeting is the period set aside for industry conferences which enable members to have separate discussion meetings on problems peculiar to their own industries.

The research work of the Controllers Institute is carried on by the Controllership Foundation. Institute members and others send the Foundation suggestions for research, educational and other projects. After a thorough search of other work in the field concerned and of current projects of other research organizations in order to prevent possible duplication, several suggested subjects are submitted to the Institute membership for vote. The final decision as to which projects will be undertaken, however, is made by the Board of Trustees of the Foundation which then allocates the necessary funds. Each research project is guided by a specially chosen advisory panel of members of the Controllers Institute and, when completed, the results of the study are published.

Although active membership in Controllers Institute of America is not open to practicing CPAs, the Institute's work is of service to them because of the contribution which it makes to the development of sound techniques in the dynamic field of business management.

The Institute of Internal Auditors

The Institute of Internal Auditors is today the recognized professional organization in the field of internal auditing. It was organized in 1941 by a group of twenty-four men who felt that an organization was needed to develop the true professional status of internal auditing and to provide a medium for the interchange of ideas and information among those engaged in its practice. Growth in membership in the Institute has been steady, until today it exceeds 2,500 and includes representatives of every field of private and governmental enterprise. From the beginning, membership has been restricted to those who are directly concerned with internal auditing, in the belief that such a limitation is necessary if the organization's activities are to continue to be focused on its original objectives. However, the community of interest between internal auditors and certified public accountants has been recognized by the Institute since its formation, and it has made provision for the admission, as associate members, of CPAs as well as eligible educators and others engaged in fields related to internal auditing.

The maximum value of Institute membership comes with participation in the activities of a local chapter group. The first chapter was organized in New York, a little more than a year after the formation of the national body. At the close of the Institute's tenth year there were forty chapters, including four in Canada, two in the Philippine Islands, and two in
Europe. Most of the chapters hold monthly meetings, and a number of the larger ones have separate meetings of technical study groups. In addition, there are three regional conferences and a conference of the entire organization each year.

Since its foundation the Institute has been active in the field of research. Much work was done in the early years on various surveys and projects relating to audit techniques in specific industries, and in 1947 the research committee issued a statement defining the responsibilities of the internal auditor.

The importance of maintaining a close relationship between a company's internal audit department and its public accountants, to the mutual advantage of both the company and the outside auditors, has become increasingly evident in recent years. In the "Tentative Statement of Auditing Standards," published in 1947 by the committee on auditing procedure of the American Institute of Accountants, it is stated that "Where an internal auditing department exists the independent auditor very properly accords that fact appropriate weight in selecting and applying his auditing procedures. The advantages of strong internal auditing departments are becoming better recognized by many concerns of sufficient size to warrant maintaining such an organization." Because the work of a functioning internal audit department is helpful to the public accountant, all the activities of the Institute of Internal Auditors which are aimed at improving methods and winning wider acceptance by management are of benefit to him.

**Student Organizations**

There are some organizations composed of students of accounting in the colleges and business schools. Some, in the form of college professional fraternities, are national in scope; most school accounting clubs or societies are local. Some state societies of certified public accountants have established student affiliates or junior memberships.

Since such organizations are potentially effective media for developing an informed interest in the profession, members of the profession would do well to encourage and aid in their sound development.

**PROFESSIONAL LITERATURE**

The rapid advancement of the accounting profession in recent years has been due in no small part to the development of a professional literature adapted to the particular needs of American business. Without such a medium for the promulgation of current developments in accountancy practice, the present widespread uniformity of techniques and standards could not have been attained.

While the needs of each accountant vary according to the types of business which he serves, there are certain sources of information with which
all should be familiar. Some of them are periodicals or bulletins dealing with specific subjects, and some are standard texts. Most textbooks, by their very nature, deal in a generalized manner with a description of principles or procedures rather than with the wide variety of differing situations encountered in actual practice. It is the current periodicals, releases, and bulletins of the American Institute of Accountants, of other accounting organizations, and of regulatory bodies which keep the practitioner up to date on the methods of handling the varied problems which arise because of the complex structure of today's business. It is not feasible to present in this chapter a lengthy bibliography of the books and periodicals which comprise the literature of accounting. The average CPA is primarily interested in knowing which of the many available publications will be most useful to him in his practice. Reference to some worth-while literature will have been omitted, but a conscientious attempt has been made to provide representative, although limited coverage. Some of the principal periodicals and publications of these organizations will be mentioned in the following pages; textbooks are listed on pages 37-45, together with a list of the addresses of the publishers referred to.

**Institute Publications**

The official publication of the American Institute of Accountants is *The Journal of Accountancy* which is published monthly. An editorial in the first issue, published by the Institute's predecessor organization in November 1905, stated:

"The editors present the first issue of *The Journal of Accountancy* to the American accountants in the belief that this magazine marks the beginning of a movement which has for its object the establishment of accountancy in law and opinion as a learned profession."

That this movement has been successful has been adequately illustrated by the discussion of the Institute's growth. The rise in circulation of *The Journal*, which today is distributed not only to all Institute members, but to over 40,000 other subscribers as well, is a further indication of this success. In addition to presenting timely comment by the editors and articles by leading accountants and other authorities in their particular fields, *The Journal* conducts several regular departments designed especially to be of use to the CPA in his practice.

As an added means of keeping its members in touch with professional happenings, the Institute publishes a monthly internal membership bulletin, *The CPA*. Through its wide news coverage members are informed of recent developments which affect their interests in any way.

From time to time, the committees on accounting procedure and auditing procedure of the Institute issue formal pronouncements which are recognized by the profession as the most authoritative statements on the subjects involved. The Accounting Research Bulletins, which deal with
general accounting principles and their application to specific matters, summarize studies made by the committee on auditing procedure. The pronouncements of the committee on auditing procedure were originally issued as Statements on Auditing Procedure. In 1951 a single pamphlet, replacing the twenty-four statements issued up to that time, was published. This booklet, entitled “Codification of Statements on Auditing Procedure,” consolidates the more valuable and currently useful features of the previous pronouncements and is intended as a supplement to the material contained in other publications of the committee on auditing procedure and in auditing texts.

In 1947 the committee on auditing procedure issued a special report which was published under the title “Tentative Statement of Auditing Standards – Their Generally Accepted Significance and Scope.” At the 1948 annual meeting of the Institute the summarized statement of auditing standards contained in this report was approved by the membership. It is important to note that this statement is concerned primarily with auditing standards, as differentiated from auditing procedures. The committee believes that the most satisfactory method of presenting auditing procedures is by a series of case studies illustrating audit procedures adopted and applied in actual examinations. Up to the date of the publication of this Handbook, ten Case Studies in Auditing Procedure have been issued (two in No. 8), describing the audit procedures actually followed by practitioners in examinations of the following types of business organizations:

1. A Loading and Hauling Equipment Manufacturer
2. A Newspaper Publisher
3. A Department Store
4. A Public Utility
5. A Corn Processing Company
6. A Management Investment Company of the Open-End Type
7. A Grain Company
8. A Steel Fabricating Company
   A Small Restaurant
9. A Wholesale Distributor of Newspapers and Magazines

The committee on auditing procedure also has made a comprehensive study of internal control. The results of this study were published in 1949 under the title “Internal Control – Elements of a Coordinated System and Its Importance to Management and the Independent Public Accountant.” A series of case studies in internal control has since been instituted, and up to the date of the publication of this Handbook two studies have been issued, dealing with (1) The Textile Company, and (2) The Machine Manufacturing Company.

In 1949 the research department of the Institute, with the advice of the committee on auditing procedure, issued a pamphlet entitled “Audits by Certified Public Accountants – Their Nature and Significance.” This
booklet, which is designed for the use of credit executives and others concerned with the work of the independent certified public accountant, describes in general terms what the CPA does in order that he may express an opinion on financial statements.

In 1951 the public relations department of the Institute prepared a pamphlet entitled "Your CPA's Responsibility" to explain Auditing Procedure Statement No. 23 to the clients of smaller CPA firms. Another public relations leaflet issued in 1951, "Why CPA Standards Are Important to You," answers some of the questions most frequently asked about certified public accountants and their professional standards. The pamphlet entitled "Small Business Has Big Problems," which was published in 1949, outlines some of the services which CPAs can perform for smaller businesses.

In 1940 the Institute published a booklet outlining an audit program for savings and loan associations. This booklet was an important factor in raising the standards of independent audits of these associations but, with the passage of time, new developments in their accounting practices took place which were not covered. In 1951, therefore, a revised edition of the booklet, under the title "Audits of Savings and Loan Associations by Independent Certified Public Accountants," was issued by the committee on auditing procedure.

In 1946 the Council of the Institute initiated a long-range program for the analysis of corporate reports. Each year since then the research department has reviewed hundreds of these reports and has published a survey showing the manner in which various items are treated in the financial statements. This survey, which is entitled "Accounting Trends & Techniques in Published Corporate Annual Reports," points up, by means of numerous comparative tabulations, significant accounting trends during the period since the studies were started. Special attention is given in each edition to matters which have been under consideration by the committee on accounting procedure.

A pamphlet published by the Institute under the title "The Natural Business Year — Its Advantages to Business Management" contains a chart to be used in determining a company's natural business year as well as a list of suggested fiscal closing dates for different types of business.

Each year the Institute publishes the complete text of all technical papers and committee reports presented at the annual meeting. It also publishes from time to time various pamphlets, all of which are designed to promote a general recognition of the professional stature of certified public accountants.

**Publications of Other Organizations**

**American Accounting Association**

The major publication of the American Accounting Association is the official quarterly journal, the *Accounting Review*, which was first issued
in 1926. Articles in the Review cover practically the entire range of accounting subject matter. However, some attempt is made to feature articles on current developments in accounting theory, as contrasted with those of more specialized technical significance. Papers presented at the annual meetings of the Association also are included in the Accounting Review.

From time to time the American Accounting Association publishes research monographs, as well as special studies of various kinds. A research monograph entitled "An Introduction to Corporate Accounting Standards" by W. A. Paton and A. C. Littleton, which was originally published in 1940, was reprinted in 1951. In 1936 the executive committee of the Association issued "A Tentative Statement of Accounting Principles Affecting Corporate Reports." The second revision of this statement, published in 1948, is entitled "Accounting Concepts and Standards Underlying Corporate Financial Statements." Since 1948, the committee on concepts and standards of the Association has issued a number of "Supplementary Statements" dealing with various individual accounting subjects.

**National Association of Cost Accountants**

The official publication of the National Association of Cost Accountants is the *N.A.C.A. Bulletin* which is issued monthly in two sections. The first section of each issue is devoted to technical information, and the second section provides news and information on the activities of the Association and recent developments of interest to industrial accountants, as well as a review of books and articles in the field of current cost literature. The results of the studies made by the research staff of the Association are published from time to time in a special section of the Bulletin.

Each year the National Association of Cost Accountants publishes a volume entitled "Conference Proceedings" which contains a complete report of all papers and discussions presented at the annual conference. These papers cover practical cost and accounting information on a variety of subjects.

**Controllers Institute of America**

The Controllers Institute of America publishes a monthly magazine, *The Controller*. It also publishes pamphlets from time to time. While some of these deal solely with the functions and contributions of controllers, there are others, such as "Replacement Costs and Depreciation Policies" and "Tax Principles and Problems," which concern problems of more widespread interest.

The Controllership Foundation, which carries out the research program of the Controllers Institute, issues a monthly bulletin, *Controllership*
Research, giving progress reports on its projects. Like the pamphlets of the Controllers Institute, several of the special reports of the Foundation, which are based on its research studies, deal with information that is particularly useful to controllers. One of the Foundation’s reports, published in 1948 under the title “Depreciation Policy When Price Levels Change” constitutes a source book of opinions and information published up to that time on the subject.

Institute of Internal Auditors

The Institute of Internal Auditors publishes a quarterly periodical, The Internal Auditor, which was started in 1944. Prior to 1949 both technical papers and Institute news were contained in each issue. Since that time, however, a separate publication, the Members News Bulletin, has been devoted to news items. The Institute also has published several books on various phases of internal auditing, and each year it issues a volume containing the complete text of all papers presented at the annual meeting.

Government Publications

Government publications cover a wide variety of subjects. Of those which are concerned with accounting matters, some are of interest to certain accountants and not to others, depending upon the types of business which they serve. For example, accountants with clients whose accounting methods are under the jurisdiction of regulatory authorities such as the Federal Power Commission, the Federal Communications Commission, and the Interstate Commerce Commission must use the current uniform systems of accounts prescribed by them. In addition, these accountants will be interested in the periodic releases and annual reports of the commissions. Regardless of the types of business represented in his practice, however, every accountant must keep abreast of the rules, regulations and official releases of the Securities and Exchange Commission. The series of accounting releases, which are incorporated by reference in Regulation S-X, contain the opinions expressed from time to time by the Chief Accountant on controversial questions arising in connection with registration statements and annual reports filed with the Commission. Information on current developments in accounting and auditing also is included in the Commission’s annual reports which outline its activities under the different statutes entrusted to it.

The Treasury Department issues many publications, such as the fortnightly Internal Revenue Bulletin, which supplement the Federal tax service. The Excess Profits Tax Act provides for the use of certain industry classifications which, under the regulations, are to be determined in accordance with the specifications shown in the “Standard Industrial Classification Manual,” prepared by the Division of Statistical Standards
of the Bureau of the Budget.

The Department of Commerce publishes a monthly Bulletin of Commerce which contains material that is of interest to businessmen and is available without cost. Bulletins also are issued from time to time on many types of business and on methods of record-keeping for different businesses.

In 1951 the Superintendent of Documents published a booklet entitled "Suggestions for Improving the Language of Audit Reports." These suggestions were prepared by the report editor of the Corporation Audits Division, General Accounting Office for the use of that division. However, the booklet contains a great deal of information which can assist certified public accountants in the writing of more effective reports.

**Tax and Financial Publications**

The CPA Handbook chapter on "Income Tax Practice" contains a section on recommended books and services for a tax library. At this point, therefore, the listing of tax publications will be limited to the following periodicals:

*The Tax Barometer*
Published weekly by Washington Publications, Inc.

*Taxes, The Tax Magazine*
Published monthly by Commerce Clearing House, Inc.

*What's Happening in Taxation and Government Regulation*
Published weekly by Prentice-Hall, Inc.

Every accountant, regardless of the size of his practice, needs to have dividend guides and stock and bond quotation records available for ready reference. Such records are published by Moody's Investors Service and by Standard & Poor's Corporation, among others. Moody's also publishes five yearly manuals which contain detailed historical financial information.

**Reference Books**

The accountant's library should include the standard reference works — an unabridged dictionary, an encyclopedia, almanacs, and directories of various types. The "Accountants' Handbook," the "Cost Accountants' Handbook," and the "Financial Handbook" furnish the accountant with a wealth of authoritative information. His library also should include the Federal and state tax services and any other services which can assist him and his clients in complying with government regulations.

Every accountant's library should include "The Accountants' Index," published by the library staff of the American Institute of Accountants. This index provides a key to all works on accounting published in the English language. Material published up to the year 1920 was indexed in
Suggestions for a Library

The accountant’s library should be built around a core of reference books, standard texts on accounting and allied subjects, and periodicals which are of general interest to the profession as a whole. Once his library is satisfactorily equipped with publications of these types, each practitioner should endeavor to add to it such sources of information as will be helpful to his particular practice. In order to understand the problems of his clients in various lines of business, he should refer to technical periodicals, trade papers, and statistical data published by trade associations. Published corporate reports, prospectuses, and stock-listing applications should not be overlooked either, for they furnish a wealth of information on current thinking in the accounting profession.

There are many excellent texts in accounting, auditing, and related subjects, but naturally each practicing accountant will not find it necessary or feasible to include all of them in his library. All members of the American Institute of Accountants may borrow, either by mail or in person, from the Institute’s library of over 41,000 books, periodicals and pamphlets. The books suggested in Appendix A to this chapter as suitable for inclusion in an accountant’s library include representative texts dealing with the major topics of general interest to the accounting profession. Of course, this list is not intended to be either definitive or exhaustive. In some instances, the books listed for a particular subject are the most recent ones published in that field, and for this reason they have been given preference over earlier texts which, however, may deal equally well with the subject. In order to furnish a guide to accountants who, because of the nature of their practice, require books on specialized accounting, some books of this type have been included in this list. However, most of the available information on specialized types of accounting is published in periodicals, such as The Journal of Accountancy, the N.A.C.A. Bulletin, and the publications of the state societies. An extensive bibliography of specialized accounting literature is contained in J. K. Lasser’s “Handbook of Accounting Methods” and in his “Handbook of Cost Accounting Methods.” In addition, information which has been published on any phase of specialized accounting can be located through “The Accountants’ Index.”
RECOMMENDED 100-VOLUME LIBRARY

(Those titles marked * are suggested for a library of approximately fifty volumes)

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<tr>
<th>Author</th>
<th>Title</th>
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<td>Accountants' Index (Supplements published biennially.)</td>
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<td>•May, George O.</td>
<td>Financial Accounting, 1943</td>
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<td>*Paton, W. A. and Littleton, A. C.</td>
<td>An Introduction to Corporate Accounting Standards, 1940</td>
<td>American Accounting Association</td>
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</table>

**Auditing**


**Budgeting**


Rautenstrauch, Walter and Villers, Raymond Budgetary Control, 1950 Funk & Wagnalls Co.

*Sinclair, Prior* Budgeting, 1934 The Ronald Press Co.

*Wellington, C. Oliver* Primer on Budgeting, 1949 D. Van Nostrand Co.
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<td><strong>Business Organization and Management</strong></td>
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<td>National Association of Credit Men</td>
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<td><strong>Internal Audit and Control</strong></td>
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<td>*Brink, Victor Z.</td>
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<td>Brink, Victor Z. and Cadmus, Bradford</td>
<td>Internal Audit in Industry</td>
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<td>Richie, William E.</td>
<td>Production and Inventory Control, 1951</td>
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<td>*Butters, J. Keith and Niland, Powell</td>
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<td>Badger, Ralph E.</td>
<td>Investment Principles and Practice, 1951</td>
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<td>and Guthmann, Harry G.</td>
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<td><strong>Profession of Accountancy</strong></td>
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<td><em>Carey, John L.</em></td>
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<td>Rodey, Bernard S., Jr.</td>
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<td>Hall, Challis A., Jr.</td>
<td>Effects of Taxation — Executive Compensation and Retirement Plans, 1951</td>
<td>Harvard University Graduate School of Business Administration</td>
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<td>D. Van Nostrand Co.</td>
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<td>*Montgomery, Robert</td>
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<td>H., Taylor, Conrad B., and Richardson, Mark E.</td>
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<td>Smith, Dan Throop and Butters, J. Keith</td>
<td>Taxable and Business Income, 1949</td>
<td>National Bureau of Economic Research, Inc.</td>
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Valuation


**ADDRESSES OF PUBLISHERS**

American Accounting Association
College of Commerce and Business Administration, University of Illinois, Urbana, Ill.

American Book Company
55 Fifth Ave., New York 3, N. Y.

American Council on Education
1785 Massachusetts Ave., N.W., Washington 6, D. C.

American Hospital Association
18 E. Division St., Chicago 10, Ill.

American Institute of Accountants
270 Madison Ave., New York 16, N. Y.

Business Text-Book Publishers, Inc.
225 Broadway, New York 7, N. Y.

Clark Boardman Co., Ltd.
11 Park Place, New York 7, N. Y.

Commerce Clearing House, Inc.
214 N. Michigan Ave., Chicago 1, Ill.
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<td>Controllers Institute of America</td>
<td>1 East 42nd St., New York 17, N. Y.</td>
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<td>Cornell University Press</td>
<td>124 Roberts Place, Cornell Heights, Ithaca, N. Y.</td>
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<td>The Foundation Press, Inc.</td>
<td>268 Flatbush Ave., Brooklyn 1, N. Y.</td>
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<td>Funk &amp; Wagnalls Co.</td>
<td>153 East 24th St., New York 10, N. Y.</td>
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<td>Harvard University Graduate School of Business Administration</td>
<td>Soldiers Field, Boston 63, Mass.</td>
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<td>The Institute of Internal Auditors</td>
<td>120 Wall St., New York 5, N. Y.</td>
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<td>Richard D. Irwin, Inc.</td>
<td>1818 Ridge Road, Homewood, Ill.</td>
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<td>Louisiana State University Press</td>
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<td>McGraw-Hill Book Company, Inc.</td>
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<td>Municipal Finance Officers' Association</td>
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<td>70 Fifth Ave., New York 11, N. Y.</td>
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Practical Applications of Professional Ethics

BY JOHN L. CAREY

Executive Director of American Institute of Accountants

A code of ethics is a practical working tool. It is useful to a professional practitioner in the same sense that his theoretical principles and technical procedures are useful. Without a system of professional ethics he would be incomplete.

Professional ethics form a small part of a great, complex system of discipline which civilized society has imposed on itself through laws, customs, moral standards, social etiquette—rules of many kinds enforced in many ways. Discipline is necessary, if people are to live together in large numbers, to restrain the primitive animal instincts with which man is born.

The assurance that such discipline exists is also the basis of man's faith in his fellow man, which, despite frequent disappointments, is essential to the continuation of the highly involved and ramified economic structure which now supports most of the free world's population. Credit and investment are the underpinning of that structure, and they rest to a greater extent on faith in moral standards, and ethical considerations, than on the formal law. There could never be enough policemen to enforce the laws if all the people chose to violate them at one time. A code of professional ethics is a voluntary assumption of the obligation of self-discipline above and beyond the requirements of the law. It therefore serves the highly practical purpose of notifying the public that the profession intends to do a good job in the public interest. In effect, the existence of the code suggests that in return for the faith which the public reposes in members of the profession, they accept certain obligations to behave in a way that will be beneficial to the public. This is so obviously good business, aside from any higher considerations, that one wonders why certified public accountants have not publicized their rules of professional conduct more widely. The rules should be familiar to every client, to bankers and credit men, to lawyers and others concerned with certified
public accountants, simply as a matter of public relations.

The ethical code also serves the highly practical purpose of providing members of the profession with guides to the type of behavior which the historical experience of the group as a whole has indicated is most likely to attract the confidence of the public.

The reason such guides are needed is that natural human instinct and common sense, and even a fine sense of right and wrong, are not always enough to point out the best way for a professional man to behave in a given situation. His relations with other people can be extraordinarily complicated, and sometimes it is best for him to behave in a way that would seem unnatural and even illogical to others.

When people need a doctor, or a lawyer, or a CPA, they seek someone whom they can trust to do the best he can — not for himself, but for them. They have to trust him, since there is no practicable way to appraise the quality of his “product.” And so they must believe that his primary motive is to help them.

That is why professions are distinguished from businesses — and why professional men are looked up to with respect.

Professional men are accepted as men highly skilled in some science or art, who desire to minister to other people — who want to serve the public, and who place service ahead of personal gain. If they were not regarded in this light they would have no patients or clients. Who would engage a doctor, or a lawyer, or a certified public accountant who was known to put personal gain ahead of service to his patient or client? How could anyone know whether to take his advice or not? If the practitioner were mainly interested in selling his services and building up fees, he might be expected to keep his patients sick, or keep his client in litigation, or extend his examination of the clients’ accounts beyond the necessary scope. Who would engage such a man?

Not only must people believe that the professional man will not take advantage of them financially, but also that they can safely entrust him with their most private and vital affairs. He must be regarded as a man of character. So he must behave himself in a way that strengthens their confidence. He must display a professional attitude toward his work.

A professional attitude must be learned. It is not a natural gift. It is natural to be selfish and greedy — to place personal gain ahead of service. (That is precisely why the people as a whole honor the relatively few — like professional men and other true public servants, who have disciplined themselves to follow the nobler way.) A professional attitude, like a golf swing, must be acquired by self-discipline. The rules of ethics are guides to right action — to action that will develop the professional attitude, and thus win public confidence.

Now, public confidence is even more important to a certified public accountant than to other professional men. He must have not only the confidence of those who become his clients, but also the confidence of
those who rely on his reports. His service may be of little value to a client if a bank will not accept his report. And the bank, or the credit agency, or the government agency, or other "third parties" who may rely on the report, will accept it only if they believe that the CPA feels a responsibility to look out for their interests as well as the client's.

And since all the multitude of "third parties" who may rely on the reports of certified public accountants are not likely to know the CPAs personally, this means that they must have confidence in CPAs as such—in the whole accounting profession—as men who can be trusted to do a good job for all concerned.

So, the rules of professional conduct of the accounting profession serve highly practical purposes:

1. They show the practitioner how to maintain a professional attitude which experience indicates will help him to succeed.
2. They give clients and potential clients a basis for confidence that CPAs sincerely desire to serve them well, and place service ahead of reward.
3. They give "third parties" who may rely on financial statements a basis for confidence that the CPA has done his work in conformity with objective standards and is independent in expressing his opinion.

The best way of demonstrating the practical value of a code of ethics, perhaps, is to imagine that it did not exist. Suppose each practitioner had to decide for himself, in the light of his own particular training and experience, what would be the best way to behave in any of the situations in which he might find himself. It would be too much to expect that everyone would perceive the right answers. The professional attitude would be likely to disappear rapidly. Public accounting would come more and more to resemble a business service. Public confidence would correspondingly decline, and eventually some other means would have to be found to provide "third parties" who risk money on financial statements of business enterprises with some evidence of the reliability of such statements. In view of the present trend of society, it may be presumed that this would be accomplished through audits by government staffs. The practice of accounting would remain only to the extent that businesses not large enough to employ competent accountants on a full-time basis made use of accounting firms to help them with their internal administrative accounting problems.

While the Rules of Professional Conduct of the American Institute of Accountants are officially stated in chronological order of adoption, they may be grouped according to subject matter quite conveniently around the following three objectives:

**Professional Attitude**

1. Firm name, style, and descriptions must be appropriate.
2. Practice as a corporation is forbidden.
3. Occupations incompatible with public accounting are prohibited.
4. Members in practice but also engaged in other related occupations must also observe rules of conduct in such occupations.
5. Advertising is prohibited.
6. Solicitation is prohibited.
7. Institute members must observe state rules on competitive bidding.
8. Offers of employment to employees of other accountants are prohibited.

Confidence of Clients
1. Confidential relationship with client must not be violated.
2. Splitting fees or paying commissions to laity is prohibited.
3. Member may not permit another to use his name except his partners and employees.
4. Member may not sign work prepared by others than his own associates or other accredited accountants.
5. In certifying statements members must conform with generally accepted accounting and auditing standards.

Confidence of Third Parties
1. In certifying statements, accountants must conform with generally accepted accounting and auditing standards.
2. Contingent fees in conjunction with audit work are prohibited.
3. Members must not vouch for the accuracy of forecasts of earnings.
4. Member may not express opinion on financial statements of an enterprise financed by public distribution of securities if he, or one of his immediate family, has a substantial financial interest in the enterprise; if the enterprise is not publicly financed but the statements are used as basis of credit, he may not express an opinion unless in his report he discloses any substantial financial interest which he, or his family, may have in that enterprise.

It is immediately evident that the present rules do not deal with all the ethical questions which may arise in the practice of public accounting.

The basic ethical concept of independence, for example, is not nearly so fully presented in these rules as it has been in literature of the profession. Many specific ethical questions not covered in the rules have been answered in opinions of the Institute's committee on professional ethics.

Still other ethical questions have not yet been answered decisively at all. The evolutionary processes of accumulating wisdom are still at work.

The remainder of this chapter is devoted to specific questions of ethics likely to be encountered in practice. The answers are based on the best authorities available — sometimes a rule, sometimes a committee opinion, sometimes only a published article.

Authorities are indicated as follows: RPC — Rules of Professional Conduct, American Institute of Accountants; CE — opinion of Committee on Professional Ethics, American Institute of Accountants; other sources are named in full.

Space does not permit consideration of all questions that may arise, nor full discussion of the reasoning underlying the answers. More extended discussion of some of these matters may be found in "Professional Ethics of Public Accounting." ¹

¹ See reference 1 at end of this chapter.
The purpose here is to provide the quickest possible answers to the most common practical questions of professional ethics.

FORMS OF ORGANIZATION AND DESCRIPTIONS

1. Can an individual certified public accountant style himself as "John Doe and Company"?

The Institute's rules do not prohibit such a description, but Treasury Department Circular 230, which applies to all agents enrolled to practice before the Treasury, does contain such a prohibition. Section 10.2 (e) of Circular 230 says: "Every enrolled attorney or agent practicing as an individual shall use his legal name in the conduct of his legal, accounting, or other professional practice. The term 'company,' 'associates,' 'accountants,' 'auditors' . . . or other plural forms suggesting a partnership, or language of similar import, used in connection with a name or title, or any fictitious title, or trade name, shall be used only by a bona fide partnership consisting of two or more members, and all stationery, listings, advertisements, and announcements of enrolled persons shall conform to the principles herein stated."

Rule No. 1 of the Rules of Professional Conduct (RPC) states that an individual practicing under a style denoting a partnership when in fact there is no partner or partners shall not use the designation "members of the American Institute of Accountants."

Most state accountancy laws contain provisions similar to Rule No. 1 with respect to the use of the designation "certified public accountants"; that is, the designation may not be used unless a partnership actually exists (and, of course, all the partners are certified public accountants).

2. What types of firm name or "style" are appropriate for a partnership?

The following are appropriate:

Smith & Jones
Smith & Company
The John Smith Company
Smith & Associates

The committee on professional ethics (CE) has held that the name of a firm of practicing accountants should denote a personal association. Such a firm should not adopt for its name any nonpersonal or misleading title. A corporate form of name, such as "Unique Audit Company" would not be appropriate as the name of a firm of professional accountants.

3. How can a partnership of CPAs describe itself?

The designation "certified public accountants" may be used in conjunction with the firm name, if all the partners are certified public accountants of the state in which the firm practices. If some partners are certified in one state and some in another, then the laws of the state in
which the practice is being carried on should be consulted — provisions differ among the several states.

If all the partners of the firm are members of the American Institute of Accountants, the designation "Members, American Institute of Accountants" may be used in conjunction with the firm name.

If some of the partners are members of the Institute and others are not, the designation may not be used in conjunction with the firm name, but the names of the individual partners who are members may be listed in the corner of the letterhead with the designation "Member, American Institute of Accountants" following each name as appropriate.

Occasionally a firm may wish to show on its letterhead the names of accountants with the firm who are not partners. The CE has approved the listing of both partners and staff, provided the partners are shown first in order, followed by a line to separate them from members of the staff who may be named. In this way, the public is put on notice that those below the line have some other status than that of partner.

4. Can certified public accountants practice public accounting in the corporate form of organization?

No. RPC No. 11 says a member shall not be an officer, director, stockholder, representative, or agent of any corporation engaged in the practice of public accounting in any state or territory of the United States, or the District of Columbia.

Most state accountancy laws also forbid practice in the corporate form.

5. Can a certified public accountant practice in partnership with a CPA of another state?

Generally, yes, but the laws of the states in which offices are to be maintained should be consulted. Under some "regulatory" laws it is necessary for all members of a partnership practicing in a state to be registered, and particular attention should be paid to the statutory provisions related to use of the designation "certified public accountants" in conjunction with the firm name.

6. Can a certified public accountant practice in partnership with a noncertified public accountant?

There is nothing in the rules of the Institute which would prevent a member from entering into partnership with a noncertified public accountant.

There is nothing in most CPA laws to prevent the partnership of a CPA with a non-CPA. However, in "regulatory" states, the noncertified accountant would have to be registered and licensed to practice accounting in the state.

Naturally, the description "Members, American Institute of Accountants" or "certified public accountants" would not be permissible in conjunction with the firm name of a partnership composed of a certified
public accountant and a noncertified public accountant.

The letterhead of a firm composed of both certified and noncertified public accountants may show the names of individual partners, and in this case the designation CPA may follow each name entitled to it.

It should be borne in mind in a partnership of this type that the CPA is ethically responsible for all the acts of the partnership. In other words, if his noncertified partner should violate the Rules of Professional Conduct, the CPA would be held accountable.

The Canons of Ethics of the legal profession do not permit partnerships between lawyers and “laymen.” The rules of the Institute of Chartered Accountants in England and Wales permit a chartered accountant to form a partnership only with another chartered accountant. It has been suggested that similar restrictions should be imposed upon CPAs in the United States, but no action has been taken.

7. Can a CPA practice public accounting in partnership with a lawyer, an engineer, or a member of another profession?

The rules of professional conduct of the Institute have not been construed to prevent such a partnership. It should be noted, however, that the legal profession frowns on partnerships between lawyers and non-lawyers, and in no event could the CPA practice law unless he is also a lawyer and practices as such. Again it should be noted that in “regulatory” states only accountants registered and licensed to practice may engage in public accounting and it would therefore not be appropriate for a CPA to associate himself in partnership with a lawyer or an engineer for the practice of public accounting unless the lawyer or engineer also were registered as a public accountant.

Again it should be noted that the CPA would be responsible for any violations of the Rules of Professional Conduct on the part of his non-accountant partner.

8. Is it ethical to buy a public accounting practice?

The purchase of public accounting practices has been, and continues to be, a generally accepted method of acquisition. There has been no intimation by any of the professional accounting societies that there is anything unethical about it.

9. Is it ethical to pay the estate of a deceased partner a share of the profits of the partnership over an agreed period?

RPC No. 3 forbids participation by the “laity” in fees or profits of professional work, but the CE has held that payments to a widow or the estate of a former partner would not be considered a violation of that rule. It would be improper, CE has held, for a former partner’s widow to be included as a partner of a firm of certified public accountants (unless she were personally professionally qualified).

10. Is it ethical to practice under a firm name composed of the names
of persons who are no longer partners of the firm?

Inclusion in the firm name of the name of a former partner or former partners has been held by the Council of the American Institute of Accountants to be entirely appropriate.

11. May the sole survivor of a partnership continue practice as an individual under the old partnership name?

This apparently would be a violation of Treasury Department Circular No. 230, which provides that a firm name suggesting a partnership shall be used only by a bona fide partnership consisting of two or more members.

The CE has expressed the view that it would be improper for an individual CPA to practice under the name of a deceased CPA. It was suggested in such a case, where the goodwill had been purchased from the estate, the purchaser, who would practice in his own name, might show on his letterhead that he was successor to the deceased accountant.

The designation "certified public accountants" or "Members, American Institute of Accountants," used in conjunction with the firm name, would be inappropriate if in actuality the practice were being conducted as a sole proprietorship.

12. Is it proper to practice in association with another accountant without any actual partnership arrangement?

There is nothing in RPC which would prohibit the sharing of office space by two certified public accountants not actually in partnership, nor is there anything in the rules to prohibit two such certified public accountants from assisting one another in the conduct of engagements from time to time. Such arrangements, however, should be specific and a matter of record. Each CPA should be compensated by the other for whatever time he might spend in assisting the other.

Loose arrangements of this sort might lead to violation of RPC No. 2, which states that a member shall not allow any person to practice in his name who is not in partnership with him or in his employ. If the association is between a CPA and a noncertified public accountant, then the CPA should also be aware of Rule No. 6, which states that a member shall not sign a report purporting to express his opinion on the result of examination of financial statements unless they have been examined by him, a member or an employee of his firm, a member of the Institute, a member of a similar association in a foreign country, or a certified public accountant of a state or territory of the United States or the District of Columbia.

13. What information may properly appear on letterheads, cards and legends on office doors, windows, and building directories?

Such information should be restricted to the name of the firm, the designations "certified public accountants," "Members, American Institute of Accountants," or similar designations, when permissible; and, if desired, the names of individual partners, and cities in which offices are
maintained, but not a listing of services rendered.

No lettering on office windows or building directories or signs of any kind should be so large or prominent as to constitute in effect "display advertising."

ANNOUNCEMENTS

1. What type of announcements may certified public accountants have published in newspapers or magazines?

RPC No. 10 provides that announcements may be published in newspapers or magazines only for the purpose of announcing a change of address or a change of personnel of firm. This is construed to include the announcement of the opening of a new office by a new firm.

A change of personnel of firm is considered to mean a change in the partnership, not in the staff.

Such announcements are not to exceed two columns in width and three inches in depth if appearing in a newspaper, and are not to exceed one-quarter of a page if appearing in a magazine or similar publication.

The information which may be included in the announcement is the name; designation, such as "Member, American Institute of Accountants," "CPA," or other professional affiliation; class of service; and address of the person or firm.

In describing "class of service" it should be borne in mind that the designation "tax consultant," and similar designations, have been held to be improper by the National Conference of Lawyers and Certified Public Accountants in a Statement of Principles which has been approved by the Council of the American Institute of Accountants.

Bearing in mind that the Canons of Ethics of the bar prohibit lawyers from advertising any specialty in the law, many certified public accountants believe it desirable, even though the Institute has no similar rule, not to describe the "class of service" rendered — that is, audits, taxes, systems, et cetera. At this stage of the profession's development, it is generally felt that the description "certified public accountants" sufficiently informs the public of the nature of the services offered.

2. What type of announcements may be sent through the mails, and to whom?

Cards bearing announcements of the nature and in the form permissible for publication in newspapers or magazines (see 1 above) may properly be sent through the mails to clients and friends.

Such announcements should not be sent to complete lists of bankers, lawyers, or businessmen, or the memberships of any organization, and should not be mailed to persons who are already served by other public accountants.

The CE has ruled that it is undesirable to send such announcements to clients of a former employer.
3. What restrictions are there on listings in classified telephone directories and other directories?

RPC No. 10 provides that a paid listing in a directory should be restricted to the name, title, class of service, address, and telephone number of the person or firm, and shall not appear in bold type, box, or other form of display or in a style which differentiates it from other listings in the same directory.

The CE has held that use of the designation, “Member, American Institute of Accountants,” when used in a directory listing, differentiates the listing from others in the list, and therefore the designation should not be included.

ADVERTISING AND SOLICITATION

1. What are the restrictions on advertising?

RPC No. 10 says “A member shall not advertise his professional attainments or services.” Except for the publication of announcements as described in the preceding section, no advertising of any kind is permitted.

2. Is it permissible to publish a blind ad, not giving the name of the accountant but only a box number, indicating a willingness to accept accounting engagements?

No. CE has held this constitutes advertising professional attainments or services regardless of whether the accountant’s name appears or not.

3. Is it proper for an accounting firm to advertise for personnel?

Yes. An advertisement for staff assistants is not considered an advertisement of professional attainments or services, and it may be published with the name of the accounting firm concerned.

4. What are the restrictions on solicitation of clients?

RPC No. 7 says a member 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.

This seems to mean that a CPA may not properly solicit clients generally, may personally offer his services only when personal relationships warrant such an approach, and in no event may he solicit a client presently served by another public accountant.

The CE has not yet interpreted the phrase “warranted by existing personal relations.”

5. Is the publication of firm bulletins permissible?

Yes, but they may be distributed only to clients and staff.

Even when distribution is confined to clients, CE does not regard with favor the distribution of material prepared by commercial publishers on
which the accountant's name has been imprinted in such a way as to indicate that he prepared the material when such is not the case.

6. Is unsolicited publicity about a certified public accountant objectionable?
   No. Advertising is defined as something which is paid for by the accountant concerned. If his activities are regarded as news and they are publicized without effort on his part, he should not be accused of unethical conduct.

7. Are there restrictions on public speaking or writing for publication?
   The Institute's rules contain no such restrictions. Treasury Department Circular No. 230, however, prohibits the publication of articles or the delivery of addresses on Federal tax questions by an enrolled person in connection with which the name of the firm of which he is a member or otherwise associated or his address is given either by the writer, speaker, announcer, or publisher.

8. How can a CPA properly make himself well known in his community?
   By taking an active part in civic affairs and community organizations of all kinds, including his professional societies of certified public accountants. Publicity arising from public service activities is entirely legitimate.

9. May a CPA properly engage in politics?
   Yes. There is nothing in the Rules of Professional Conduct that denies a CPA his full rights as a citizen. Many CPAs consider it desirable for members of their profession to stand for political office, as many lawyers do. CPAs have served as mayors of their cities, as members of state legislatures, as members of the Federal Congress, as state auditors, and in other public offices.

FEES

1. Is it unethical to give an estimate of the cost of a professional service?
   No. A CPA is entitled to give a client an estimate of what he thinks it will cost — or what he thinks the maximum cost will be — to perform a specified piece of work.

   However, many CPAs refuse to submit "bids" for professional accounting engagements. An estimate may be considered a bid if it is offered in competition with other public accountants.

   Some state societies of certified public accountants have adopted rules against competitive bidding. The Institute's Rule No. 14 says that a member shall not make a competitive bid for professional engagements in any state, territory, or the District of Columbia, if such a bid would
constitute a violation of any rule of the recognized society of certified public accountants or the official board of accountancy in that state, territory, or district.

Some businessmen “shop around” in an attempt to obtain professional accounting services as cheaply as possible. Sometimes a request for an estimate of the cost of an audit may be in effect a request for a bid, because other firms are being asked for estimates at the same time.

2. Must fees be based wholly on per diem rates?

No. In computing his fee, a CPA is entitled to give consideration to all related factors—the time and effort required, the novelty and difficulty of the questions involved, the skill requisite properly to perform the engagement, the customary charges by certified public accountants for similar services, the amounts involved in the transactions to which the accountant’s work relates, the extent of the benefit to the client resulting from the accountant’s services, and the character of the employment whether casual or for an established and constant client.

3. Is there any objection to annual retainers?

No. They are generally considered desirable.

4. Is it proper to undertake an engagement on a contingent-fee basis—the amount of the fee to depend on the accountant’s findings or the results thereof?

No. RPC No. 9 says that professional service shall not be rendered or offered for a fee which shall be contingent upon the findings or results of such service.

However, the rule states that it does not apply to cases involving Federal, state or other taxes, in which the findings are those of the tax authorities and not those of the accountant.

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.

With respect to Federal income tax matters, Treasury Department Circular No. 230 permits a wholly contingent fee agreement only when the financial status of the client is such that he would otherwise be unable to obtain the services of an agent. Partially contingent fee agreements are permissible where provision is made for the payment of a minimum fee. Such minimum fee must be paid and retained without regard to the outcome of the proceedings and must be substantial in relation to the maximum fee.

5. Is it proper to accept a “forwarding fee” or “referral fee” for work referred to another accountant?

There is nothing improper in accepting “forwarding fees” so long as
they are reasonable in amount. A “forwarding fee” should not be so great as to allow only a small margin of profit to the firm doing the work. Actually, many certified public accountants will not accept “forwarding fees,” since they regard it as a favor on the part of the other accountant involved to have undertaken to perform an engagement at their request.

A “forwarding fee” paid to a nonaccountant would be a commission, brokerage, or other participation in the fees of professional work, and consequently would be a violation of Rule No. 3.

6. Is it proper to accept a fee for signing statements or reports prepared by another accountant?

No. Rule No. 6 states that a member shall not sign a report purporting to express his opinion as the result of examination of financial statements unless they have been examined by him, a member or employee of his firm, or another CPA or foreign accountant of equivalent standing.

The last exception is made in order to permit arrangements to be made through which certified public accountants in different parts of the country, or foreign accountants of equivalent standing, may examine branches or subsidiaries of corporations, and the results of their examinations may be consolidated with those of a larger group.

This type of “joint engagement” is fairly common and permits great savings in traveling expenses.

7. Is it proper for a CPA to split fees with persons not CPAs who may have helped him to secure engagements?

No. This would be a clear violation of RPC No. 3.

**RELATIONS WITH CLIENTS**

1. Is it necessary to find out how a prospective client happened to get in touch with the CPA?

While there is no rule on the subject, it is customary for all professional men to endeavor to ascertain how a new client or prospective client learned of them. One purpose is to ascertain whether or not the prospective client is “shopping around” in an effort to obtain professional services at low cost.

2. What should a CPA learn about a prospective client before agreeing to do work for him?

It is desirable to ascertain whether or not the prospective client has been or is being served by other public accountants. If so, it is desirable to learn the reasons for a change. It is considered good practice, in such a case, to request the prospective client’s permission to discuss the situation with the former accountants. If such permission is refused, it may be grounds for suspicion either that the prospective client is not financially responsible, or that he desired the former accountants to do some-
thing which they did not consider ethically proper.

In any event a CPA should satisfy himself that a prospective client is reputable and responsible and is engaged in a legitimate business; otherwise the CPA may find himself subsequently embarrassed by the association.

3. Is it ethical to discuss with a client of another public accountant, at that client's invitation, the possibility of rendering accounting services to that client?

Yes. RPC No. 7 says that a member may furnish service to those who request it. Obviously, then, he may properly respond to an invitation to discuss the possibility of furnishing such service. But it is considered good practice to communicate with the prospective client's present public accountant (see 2 on preceding page). In no event should the CPA solicit the opportunity to initiate such a discussion.

4. Is it ethical to furnish income tax system work or other services to a client whose accounts are audited by another public accountant?

Yes, if the services are furnished at the client's request, without solicitation. Such arrangements, while not common, have occurred fairly frequently.

5. Just what is meant by the "confidential relationship between CPA and client"?

It means that the certified public accountant should not voluntarily disclose information about his client which he acquired in the course of his professional service. RPC No. 16 says "a member shall not violate the confidential relationship between himself and his client."

The CE has held in one case that even if a CPA learned through performance of his professional duties of fraud or other wrongdoing on the part of his client, he could not properly report the facts to others without the client's consent, but should withdraw from the engagement and write a letter to the client stating the reasons therefor. (In some situations of this kind there may be legal responsibilities involved, and the CPA should always consult his attorney as to the proper action in view of the specific facts of the situation.) Except in some eleven states,* communications between certified public accountants and clients are not "privileged" under the law. Elsewhere the courts may compel a certified public accountant to disclose information acquired in the course of his professional service. Even in the eleven states Federal courts may not sustain the privilege, particularly in matters of Federal taxation.

Certified public accountants should make such disclosures, however, only under compulsion, and not voluntarily.

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* Arizona, Florida, Georgia, Illinois, Iowa, Kentucky, Louisiana, Maryland, Michigan, New Mexico, and Tennessee, and Puerto Rico.
6. Does the certified public accountant own his own working papers?
Yes. The Supreme Judicial Court of Massachusetts, in the case of Ipswich Mills v. Dillon \(^2\) held that the accountant's working papers are his property and not even the client can require their surrender. The laws of nine additional states \(^*\) have since made similar provision.

However, working papers may be required to be produced in court by subpoena in the absence of statutory privilege. For his own protection, it has been suggested that in such cases the accountant should make photostatic copies of the working papers for his own files.

7. To what extent does the rule against advertising restrict a CPA in sending information to his clients through the mails?
He is entitled to send his clients anything he wishes, but it is considered poor form for him to send them materials like blotters, calendars, rulers, and similar materials which might be displayed in the clients' offices and noticed by other visitors there.

As indicated previously, it is also considered poor taste to send clients material prepared by commercial publishers which bears the accountant's name in such a manner as to indicate that he is the author of such material.

8. May a CPA accept a commission from a supplier on the sale of products or services to a client at the recommendation of the CPA?
No. RPC No. 3 says that commissions, brokerage or other participation in the fees, charges or profits of work recommended or turned over to the laity as an incident to services for clients shall not be accepted directly or indirectly by a member.

RELATIONS WITH STAFF

1. Does a CPA have any ethical obligation to his staff employees?
No such obligation is mentioned in the Rules of Professional Conduct. However, it is traditional in all the professions that the practitioner has a duty to instruct his staff and to train them in the skills of the profession. Proper consideration for the health, comfort, and happiness of employees is considered a general obligation of all employers.

2. May a CPA properly offer employment to an accountant in the employ of another CPA?
RPC No. 8 says that direct or indirect offer of employment shall not be made by a member to an employee of another public accountant, without first informing such accountant.

However, a CPA is free to negotiate with any prospective employee

who, of his own initiative, or in response to a public advertisement, shall apply to that certified public accountant for employment.

Even in such cases it is considered good manners to check with the present employer of the applicant, with the applicant's consent.

3. **May a CPA employ lawyers, engineers, or other specialists as members of his staff?**

There is no provision in the Rules of Professional Conduct which would prevent it. However, the bar generally looks with disfavor on the employment of lawyers by laymen if it appears that such lawyers render legal services to others on behalf of the employer. Presumably a lawyer employed by a CPA would not be considered entitled to "practice law." He would be entitled to perform only such services as his employer was legally authorized to perform.

Naturally, a CPA employing members of other professions would be responsible for any violation of the Rules of Professional Conduct of the accounting profession by the firm as a whole or by any employee thereof.

4. **Is it proper to require staff accountants to sign agreements restricting the extent of their practice if they should leave a CPA's employ?**

There is no ethical rule governing this point. There is a difference of opinion within the profession as to whether or not such agreements are psychologically helpful. Whether or not they are legally enforceable probably depends on the facts of each case, and should be the subject of legal advice.

The committee on professional ethics has taken the position that an employee is morally bound by any agreement which he enters into voluntarily with his employer. In any event, a staff accountant, undertaking practice on his own account, is prohibited by the Rules of Professional Conduct from the solicitation of clients of other public accountants, including those of his former employer.

**INDEPENDENCE**

1. **What is the general concept of independence as it applies to public accounting practice?**

RPC do not define independence, but the Council of the American Institute of Accountants adopted a general statement on the concept in 1947 and which was published in *The Journal of Accountancy.* Boiled down, the statement says, in effect: "... Independence is traditionally associated with the CPA's function of auditing and expressing an opinion on financial statements, of vital importance to stockholders, creditors, and others who rely on such statements. ... It has become of great value to those who rely on financial statements of business enterprises that they be reviewed by persons skilled in accounting whose judgment is uncolored by any interest in the enterprise, and upon whom the obligation has been imposed to disclose all material facts."
The established rules of conduct require disclosure of all material facts, and of material departures from generally accepted accounting or auditing principles applicable in the circumstances. (RPC No. 5) The rules also prohibit a CPA from having a substantial financial interest in a company of which he is auditor, if its securities are widely held. Any such interest in a closely held company of which he is auditor must be disclosed in his report. (RPC No. 13)

"Rules of conduct," continued the Council's statement, "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."

The Securities and Exchange Commission (SEC) has given great emphasis to the concept of independence, and has adopted a rule on the subject which has been applied in a number of cases.

Full discussions of the SEC's view and of the profession's view are contained in papers delivered at the Institute's 63rd Annual Meeting in 1950: "The Concept of Independence in Accounting," by Donald C. Cook, CPA, Commissioner, SEC; and "Independence from the Viewpoint of the Certified Public Accountant," by Edward B. Wilcox, CPA, past president of the Institute.

If there is a distinction between the SEC's view and the profession's view of independence, it may, perhaps, be put this way:

The SEC emphasizes the specific relationships between an accountant and his client which give rise to a presumption of lack of independence— the SEC will not recognize an accountant as independent if any of the proscribed relationships exist.

The Institute emphasizes the fact of independence—the state of mind which the word denotes. It recognizes that an accountant may be independent in spite of close relationships with his client—or that he may lack independence in spite of the most correct appearances. The Institute, therefore, has not chosen to prohibit a great variety of relationships which might conceivably tend to introduce a subconscious bias into the accountant's judgment, but rather relies mainly on Rule No. 5 to determine whether independence has actually been impaired or not. If accepted accounting and auditing standards are observed, and all material facts are fully disclosed, it may be presumed that independence exists.

2. Specifically what relations with the client does the SEC consider to impair independence?

Because of the differing approaches of the Institute and the SEC to the question of independence, accountants whose clients must file state-
ments with SEC, and who therefore become subject to the Commission's rules, must be familiar with SEC requirements relating to independence.

SEC Regulation S-X, Rule 2-01 provides that an accountant will not be considered independent with respect to any client with which he has the following relationships:

- Substantial financial interest
- Promoter
- Underwriter
- Voting trustee
- Director
- Officer
- Employee

In specific cases, the SEC has held that the following factual situations tended to impair independence of certifying accountants:

1. Employee of certifying accountants was controller of registrant.
2. Accountants consciously falsified facts.
3. Accountant relied on unverified information furnished by client.
4. Accountant subordinated his judgment to that of client.
5. Employee of certifying accountants did much of the bookkeeping for registrant.
6. Private audit report to management differed from report made public.
7. Client and accountant made substantial personal loans to each other.
8. Close personal relations existed between accountants and management, plus various personal services by accountants for management in their individual capacities (together with other factors).
9. Accountant was officer of, and was intimately associated with, a large holding company system, of which registrant was only a segment.
10. Accountant permitted his name to be used for an account through which officers of client traded in client's stock.
11. Accountants engaged treasurer and bookkeeper of registrant to do detailed auditing work.
12. Accountants failed to make sufficient investigation of intercorporate transactions.
13. Partner of accounting firm actively participated in promotion of registrant.
15. Accounting firm acted as custodian of securities of registered investment company.
16. Accountant maintained open account, represented by cash and securities with registered broker dealer, financial statements of which accountant certified.
17. Partners of accounting firm were also partners of a law firm passing on legality of securities being issued by registrant.
18. Accountant posted to general ledger entries covering a month's transactions and made all closing entries.
19. Accountant served as salesman for securities dealer, not a client, but audited accounts of other registered securities dealers.

These examples do not cover all, or even a majority, of the actual rulings on independence by the SEC, but they do indicate the principal relationships which have been held to impair independence. The questions arising most frequently involve financial interest and employment of accountants in other capacities as well as that of auditor.

3. What relationships does the Institute regard as impairing indepen-
The Institute has specifically considered only a few of the relationships with which the SEC has found it necessary to deal.

The Institute's views on these relationships may be summarized as follows:

**Substantial Financial Interest**

1. RPC No. 13 provides that a member shall not express his opinion on financial statements of any enterprise financed in whole or in part by public distribution of securities, if he owns or is committed to acquire a financial interest in the enterprise which is substantial either in relation to its capital or to his own personal fortune, or if a member of his immediate family owns or is committed to acquire a substantial interest in the enterprise.

2. If the client is not financed by public distribution of securities, but the financial statements on which the member expresses his opinion are to be used as a basis of credit, the rule provides that the member shall disclose in his report any such financial interest as described previously.

**Service as Director and Auditor**

1. RPC are silent on this point, but CE has ruled on numerous occasions that it is unwise for an independent auditor to serve as member of the Board of Directors of a corporate client, and that if he does, the relationship should be disclosed. The New York State Society of Certified Public Accountants has a rule requiring disclosure of such a relationship.

2. It has been contended that a permissible exception may be in the case of charitable or other nonprofit organizations, but even here it must be recognized that the accountant who serves both as auditor and director assumes additional responsibility.

**Bookkeeping Service and Auditing**

1. The question has often been raised whether an accountant can appropriately express an opinion on financial statements when he has participated in keeping the client's books. SEC would probably hold that the accountant could not be regarded as independent in these circumstances. However, it can be strongly argued that the accountant's independence is not necessarily impaired by his participation in the bookkeeping.

2. This question was considered at length by the committees on auditing procedure and professional ethics of the American Institute of Accountants. The conclusion is stated in the report of the committee on auditing procedure to the Council of the Institute dated October 6, 1951 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 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."
Financial Relations with Personnel of Client Companies

1. The Council of the American Institute of Accountants, sitting as a trial board in 1941, expressed the view that all public accountants should avoid any financial relationship with officers or employees of client corporations, in the form of borrowing or lending, or participation in the profits of investments, or in any similar manner.

4. *May a CPA serve two or more clients whose interests conflict without impairing his independence?*

It is an accepted precept in the legal profession that a lawyer generally should not serve two clients whose interests conflict, and by analogy it is often assumed that certified public accountants may not properly do so either. The analogy, however, is believed to be unsound. Lawyers act as advocates, and a single lawyer could obviously not be the advocate for two opposing views. The fact that a CPA is independent permits him without impropriety to serve two or more clients whose interests may be in conflict. However, there may be circumstances in which the relationships should be disclosed to all concerned in order that there may be no misunderstanding.

This question was raised before the Council of the Institute in May 1944 with particular reference to situations in which CPAs had been called upon by governmental agencies to undertake examinations of the accounts of corporations for which the accountants had been acting as regular auditors.

The Council adopted the following resolution:

"WHEREAS, independent public accountants have been called upon by governmental agencies and others to undertake on their behalf examinations of the accountants of corporations for whom the accountants have been acting as regular auditors; and"

"WHEREAS, questions have been raised as to the propriety of selecting for such examinations the public accountants who are the regular auditors of such corporations because of the possibility of a conflict of interests; and,

"WHEREAS, independence of viewpoint is one of the essential qualifications of the public accounting profession, in that reports made by auditors for their clients are quite generally intended to be used, and are used, by third parties, such as, creditors, stockholders, directors, and others whose interests are frequently diverse;

"BE IT RESOLVED that it is the opinion of Council of the American Institute of Accountants, assembled at its regular semiannual meeting on May 9, 1944: That an independent public accountant may properly undertake accounting or auditing engagements for or on behalf of government agencies or other third parties involving the accounts of a regular client, provided his relationship to the various parties interested is fully disclosed."

**RESPONSIBILITIES OF INDEPENDENT AUDITOR**

1. *What are the ethical responsibilities of a CPA in the capacity of independent auditor in expressing an opinion on ("certifying") financial...*
These responsibilities are set forth specifically in RPC No. 5:

"In expressing an opinion on representations in financial statements which he has examined, a member may 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 materially 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 generally accepted accounting principles or to disclose any omission of generally accepted auditing procedures applicable in the circumstances."

Subparagraphs (a) and (b) require no comment.

Subparagraph (c) refers not to what the auditor does, but how he does it. If he is careless or thoughtless in planning or conducting his examination, if he relies on assistants whose competence is questionable, if he fails to exercise due professional care in the performance of his work, he may be held to have violated subparagraph (e).

The standards of adequacy in the conduct of an audit are outlined generally in Tentative Statement of Auditing Standards — Their Generally Accepted Significance and Scope, issued by the American Institute committee on auditing procedure in 1947, approved by the membership of the Institute in September 1948.

Subparagraph (d) covers two points. First, an auditor may be held in violation of the rule if he expresses an opinion on financial statements without having acquired sufficient information to warrant such expression of an opinion. In other words, he may not properly express an opinion unless the scope of his examination has been as extensive as he considers necessary to acquire sufficient information to warrant an opinion. Second, if the auditor's exceptions in his opinion relate to items in the financial statements which are so material in relation to financial position or results of operations that, with those items excluded, the opinion on the financial statements as a whole have little value, the rule may be held to have been violated. In other words, the auditor's exceptions may be considered such as to "negative the opinion."

Subparagraph (e) requires the auditor to disclose any material departure from generally accepted accounting principles or generally accepted auditing procedures.

Generally accepted accounting principles are not easy to define. They are usually considered to be embodied in the following sources:

1. Accounting research bulletins issued by the committee on accounting pro-
procedure of the American Institute of Accountants.

2. Accounting releases of the SEC.

3. Accounting opinions issued by the American Accounting Association in formal statements and monographs.

4. Authoritative literature of the accounting profession — books and articles in periodicals.

5. Proceedings of meetings of the American Institute of Accountants and other accounting societies.

6. The practices of corporations whose reports are published, as reflected, for example, in the analysis "Accounting Trends and Techniques in Published Corporate Reports" published annually by the American Institute of Accountants.

Generally accepted auditing procedures are summarized in the pamphlet entitled Codification of Statements on Auditing Procedure issued by the American Institute of Accountants in 1951. This pamphlet summarizes earlier pronouncements by the Institute's committee on auditing procedure and refers to the source material.

Authoritative textbooks and articles in accounting journals, as well as papers presented at meetings of the accounting societies, may also be accepted as sources of information on generally accepted auditing procedures.

2. What are the ethical responsibilities of a certified public accountant in permitting his name to be associated with financial statements on which he does not express an opinion?

This point is not covered in the Rules of Professional Conduct. It is the subject, however, of Statement on Auditing Procedure No. 28, issued by the committee on auditing procedure of the American Institute of Accountants and approved by the membership of the American Institute of Accountants at its annual meeting in 1949. The essential passages are as follows:

"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 to express an opinion on the statements taken as a whole. In such circumstances, the independent certified public accountant should state that he is not in a position to express an opinion on the financial statements taken as a whole and should indicate clearly his reasons therefor. To the extent the scope of his examination and the findings thereof justify, he may also comment further as to compliance of the statements with generally accepted accounting principles in respects other than those which require the denial of an opinion on the over-all fairness of the financial statements. The purpose of these assertions by the accountant is to indicate clearly the degree of responsibility he is taking.

Whenever the accountant permits his name to be associated with financial statements, he should determine whether in the particular circumstances, it is 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 cannot be expressed, the accountant must weigh the qualifications or exceptions to determine their significance. If they are not such as to negative the opinion, a properly qualified opinion would be satisfactory; if they are 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 are 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 is considered sufficient.

It is not contemplated that the disclaimer of an opinion should assume a standardized form. Any expression which clearly states that an opinion has been withheld and gives the reasons why would be suitable for this purpose. However, it is not considered sufficient to state merely that certain auditing procedures were omitted, or that certain departures from generally accepted accounting principles were noted, without explaining their effect upon the accountant's opinion regarding the statements taken as a whole. It is incumbent upon the accountant, not upon the reader of his report, to evaluate these matters as they affect the significance of his examination and the fairness of the financial statements."

The substance of Statement on Auditing Procedure No. 23 is incorporated in the previously mentioned booklet Codification of Statements on Auditing Procedure.

3. May a CPA sign a forecast of financial results?

RPC No. 12 states that a member shall not permit his name to be used in conjunction with an estimate of earnings contingent upon future transactions in a manner which may lead to the belief that the member vouches for the accuracy of the forecast.

4. May a CPA properly sign an audit report individually on behalf of the firm of which he is a partner? Does it make any difference if he is in partnership with an uncertified accountant?

The CE has expressed the opinion that it is not in itself necessarily improper for a partner of a firm who is a certified public accountant to sign reports with the firm name and below it affix his own signature with the designation "certified public accountant"—even if other partners of the firm are not certified public accountants. However, any practice which might lead the reader to believe that the firm was entirely composed of CPAs, when such was not the case, would be grounds for criticism.

5. Is a CPA required to know the accounting rules of government agencies insofar as they apply to his client's accounts?

A report issued on behalf of the Council of the American Institute of Accountants states that an accountant undertaking an examination is charged with the responsibility of familiarizing himself with accounting
or auditing requirements of government agencies empowered to prescribe rules on accounting or auditing to which the client is subject. If the accountant fails to familiarize himself with such requirements, or if he finds that these requirements have not been fairly met in the financial statements and he issues a report in which he fails to state the fact, and to take a clear exception, he may properly be subject to discipline under the provisions of the Institute's by-laws, just as fully as if the statements failed to conform to accepted accounting principles.

**COMBINING OTHER OCCUPATIONS WITH PUBLIC ACCOUNTING**

1. *May a CPA properly engage in the part-time practice of public accounting while employed on a salary by a business enterprise?*

   Yes. There is nothing in the Rules of Professional Conduct to prevent part-time practice of public accounting. It is hardly necessary to state, of course, that the CPA in this position should not undertake to conduct an “independent” audit of the enterprise by which he is employed.

2. *May a CPA combine the practice of accounting with the practice of law or engineering if he is also licensed or qualified to practice the other profession?*

   There is nothing in the RPC to prevent such a combination of practice. The committee on professional ethics of the New York County Lawyers Association has held that lawyers who are also CPAs may practice both professions in the same office. However, the corresponding committee of the American Bar Association had issued an earlier ruling which might be construed to the contrary.

3. *Are there any occupations in which a CPA may not properly engage simultaneously with the practice of public accounting?*

   Yes. RPC No. 4 says that a member of the Institute shall not engage in any business or occupation conjointly with that of a public accountant which is incompatible or inconsistent therewith. Any occupation which casts doubt on the independence of the CPA as an auditor would probably be held to be incompatible.

   The CE has held that it would be inconsistent with standards of independence and not in the best interests of the profession for a CPA in public practice to be simultaneously a limited partner of a brokerage firm engaged in the purchase and sale of securities and commodities to the public on a commission basis.

   CE has also held that a CPA in practice should not, at the same time, be an investment dealer or securities salesman.

4. *May a CPA own and operate a bookkeeping service company independently of his public accounting practice?*

   RPC contains nothing which would prevent the simultaneous conduct of a public accounting practice and the operation of a bookkeeping serv-
ice company, but Rule No. 15 provides that a member engaged in an occupation in which he renders services of a type commonly rendered by public accountants, must observe the by-laws and Rules of Professional Conduct of the Institute in the conduct of that occupation.

This means that the bookkeeping service company owned and operated by the CPA could not engage in advertising or solicitation, or otherwise be conducted in a manner inconsistent with the Institute's Rules of Professional Conduct.

5. May a CPA own or manage or teach in a private profit-making accounting or business school while also engaged in the practice of public accounting?

Yes, so long as the school conducts its operations and solicits its prospective students and advertises its courses by methods which are not discreditable to the accounting profession.

Association with a school or any other enterprise which is conducted in a manner likely to reflect discredit on the certified public accountant associated with it may be held to render him susceptible to charges of conduct discreditable to the profession.

**GENERAL ETHICAL REQUIREMENTS**

1. Are there any general ethical responsibilities imposed on the CPA not specified in the rules of conduct or brought out in the foregoing questions?

The by-laws of the Institute provide that a member may be admonished, suspended, or expelled if found guilty of "an act discreditable to the profession." While the Rules of Professional Conduct and the rulings of the committee on professional ethics enumerate many prohibited acts, they are not intended to be all-inclusive, and a member is under obligation to exercise his judgment and his conscience in doubtful areas not covered by the rules.

It may be safely assumed that any violation of the moral standards of the community would be considered as conduct discreditable to the accounting profession. In other words, a member of the accounting profession is expected not only to conform with the specific rules of conduct applicable to his profession, but also to conform with the standards of good citizenship generally accepted in his community.

The by-laws of the Institute specifically provide for the expulsion or suspension of a member who refuses or neglects to give effect to any decision of the Institute or of the Council, who is declared by a court of competent jurisdiction to have committed any fraud, or whose certificate as a CPA has been revoked or withdrawn.

**Appendixes**

Selected opinions of the committee on professional ethics are given
in Appendix A, and excerpts of the Institute by-laws and the full Rules of Professional Conduct of the American Institute of Accountants are reprinted here as Appendix B to this chapter. A selected bibliography is given in Appendix C.

References

5. loc. cit., pages 73-79.

Appendix A

SELECTED OPINIONS OF THE COMMITTEE ON PROFESSIONAL ETHICS

The following opinions of the committee on professional ethics were given in response to questions received. They have been classified under the principal rule of professional conduct which is applicable. These opinions were selected on the basis of their representing typical or common inquiries and because the answers may be helpful in interpreting the various rules:

Rule 1

1. Is it possible for a certified public accountant to become a member of a firm of public accountants, all members of which are noncertified, and at the same time retain for himself only, a practice on his own account?

There would be no violation of the Institute Rules of Professional Conduct in such a procedure. However, clients and others interested should be advised as to the dual position of the certified public accountant, to prevent any misunderstanding or misrepresentation.

2. Another member of the Institute and myself would like to form two partnerships, one in his city and one in mine. The firm in his city will be John Doe and Company, and the letterhead will contain my name in small print at the side. The firm in my city will be called Thomas Brown and Company, with his name in small print at the side. Due to our being at extreme ends of the state, we do not think one partnership would accomplish our purpose. Would this be a violation of the Rules of Professional Conduct?

There is nothing in the Institute's by-laws or Rules of Professional Conduct.
Conduct to prohibit the formation of the two proposed partnerships. The suggestion has been made that it might be desirable to have both names used in the partnership title, and designate the partnership in the city where John Doe resides as “Doe and Brown” and the partnership in the city where you live as “Brown and Doe.” Both partnerships should, of course, conform to the Institute’s by-laws and Rules of Professional Conduct.

3. **Is it proper for an accounting firm to show on its letterhead the cities in which are located firms with which correspondent relations exist, if such relationship is clearly indicated?**

There is no objection to the procedure of showing on your letterhead cities in which correspondent relations exist, provided such relationship is indicated clearly.

4. **We are an accounting firm composed of two partners, both CPAs. We contemplate organizing a new partnership composed of both partners and one staff member, to conduct business surveys and systems work, while at the same time continuing our public accounting firm. Would such a procedure be in violation of the Rules of Professional Conduct, providing the new firm were not at any time designated as certified public accountants, and would there be any objection to incorporating the new company? The business will occupy separate quarters from those of the public accounting firm, and will use a firm name of “Business Surveys and Systems.”**

There is nothing in the Rules of Professional Conduct to prevent a member from forming a partnership with noncertified public accountants to carry out accounting and system work. It is very important that such a partnership comply with Rule 15 of the Rules of Professional Conduct which provides that “A member of the American Institute of Accountants engaged in an occupation in which he renders services of a type commonly rendered by public accountants, must observe the by-laws and rules of professional conduct of the Institute in the conduct of that occupation.” Special attention is called to Rules 1, 10, and 11, which would have to be strictly complied with. The use of an impersonal name for a partnership was dealt with by the committee several years ago in the following memorandum:

“The purpose of this memorandum is to indicate the principles that should be observed by certified public accountants in partnership in choosing a firm name and style for the partnership.

The name of a firm of practicing accountants should denote a personal association. Such a firm should not adopt for its name any nonpersonal or misleading title. A corporate form of name would not be appropriate as the name of a firm of professional accountants.

Inclusion in the firm name of the name of a former partner or former partners has been held by the council of the American Institute of Accountants to be entirely appropriate.”

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5. Would there be any violation of the Rules of Professional Conduct of the Institute if a member became a limited partner of his present firm?

It might be possible to work out such an arrangement legally, but the public could hardly be expected to inquire into the details of every partnership arrangement to determine the relative liability of the individual partners with respect to the certificates issued by the firm. It would be better for the partner to sever his connections with the firm and make some arrangement to render consulting services on a fee basis.

Rule 2

The city of which I am a resident is planning to have an audit made of its accounts. A few accounting firms have been approached, but no single firm in the state has the necessary staff to properly audit the books. Most of the citizens of the city want an audit, but funds are not available to have a complete audit made. From a professional standpoint, would it be proper for several firms to submit a joint proposal to audit the accounts during the slack season at lower rates than the prevailing rates?

There seems to be no reason why the plan suggested would not be a proper one. There is nothing in the rules of conduct of the Institute to prevent any member from working for nothing if he pleases, nor is there anything to prevent the collaboration of several firms of accountants in performing a single engagement. Care should be taken to avoid violation of Rules 2 and 6, however.

Rule 3

I have been approached by a salesman of a bookkeeping service, not an accountant, to act as his professional adviser when technical problems arise. This person will make all contacts to complete sales, and will call me in to assist his customer in starting with the system. He will no doubt inform his prospective customers that he has a CPA assisting him and available for special problems. This party would be another client to me. I would have no investment in the business nor would I be considered a partner. My fee might be based on a percentage of gross income or might be based on an hourly rate. Would this sort of arrangement violate any of the Rules of Professional Conduct?

The arrangement proposed might place you in the position of having the bookkeeping service indirectly solicit business for you, and might therefore be a violation of the Rules of Professional Conduct. Your attention is directed to Rules 3, 7, and 15.

Rule 4

1. I am a practicing public accountant and have been approached by
a large insurance company with a proposition that I act as broker in handling industrial and commercial loans. This work is not with clients. However, it is possible that some of my clients would be interested in obtaining funds of this kind. Would such an arrangement be incompatible with the practice of public accounting?

Under the Rules of Professional Conduct of the Institute, you cannot act as a broker and an independent accountant at the same time. To do so would place you in violation of Rules 4 and 15.

2. I specialize in motor carrier accounting and have many contacts in that industry. A broker handling the purchase and sale of motor carrier operating rights desires to rent space in my office and work with me either on a partnership or fee basis. Mail and periodical advertising will be necessary. I will be remunerated on a fee basis for time and advice necessary to complete transactions, based upon a percentage on all completed transactions. A trade name will be used. Would such an arrangement be permitted under the Rules of Professional Conduct of the Institute?

The arrangement described would result in violation of Rules 4, 10, and 15.

3. Is it proper for an accounting firm listing itself in the telephone directory and practicing as "Certified Public Accountants" to own and operate an "Industrial Engineering Department" and as such to render industrial engineering services to the clients of other certified public accountants not owning and operating a like industrial engineering department? Is the practicing of industrial engineering simultaneously with the practice of public accounting under the same name and within the same office contrary to Rule 4 of the Institute Rules of Professional Conduct? In consideration of the fact that the state has established a State Board of Registration for Professional Engineers, which requires the licensing of all engineers engaged in public practice within the state, can it therefore be interpreted that the owning and operating of an industrial engineering department is compatible and consistent with the practice of public accounting?

An engineering or systems department in an accounting firm is not an activity that is incompatible with public accounting. Such departments in an accounting firm represented in the Institute must, under Rule 15 of the Rules of Professional Conduct, observe the by-laws and rules of conduct. Rules 7 and 10, concerning solicitation and advertising, would have to be strictly adhered to.

Rule 6

Would a member of the Institute violate professional ethics by accepting a mailing service for the confirmation of accounts receivable and
accounts payable? The service would be to mail requests for confirmations for accounting firms. The returned confirmations would be removed from the envelopes and returned to the public accounting firm.

A member of the Institute would be in violation of Rule 6 if he subscribed to such a service, in that he would be relying for an important and essential feature of his examination upon the work of another upon whom he had no right to rely. Another objection to such a plan would be that information relative to the client's affairs would be disclosed to a third party without the client's knowledge or consent, in violation of Rule 16.

**Rule 7**

1. I am now employed as a staff accountant with a firm of certified public accountants, and am contemplating entering public practice under my own name. Would there be any violation of the rules of conduct if I sent announcements to clients of the firm by which I am now employed, such clients having indicated that they would like me to continue to do their work, as well as to personal friends and acquaintances?

Announcements may be sent to personal friends and acquaintances, but the sending of such a card to clients of a former employer would be a violation of Rule 7 of the Rules of Professional Conduct.

2. For eight years we have had a refinery and its subsidiaries as a client. Due to a reorganization several years ago, the controlling stock interest of the client-company was acquired by an oil company in another state, and this last year the oil company was acquired by another company. The company which has acquired the refinery and oil company is the client of one of the large national accounting firms. Would it be contrary to the rules of conduct of the Institute for my firm to write to the petroleum company and possibly to the accounting firm, in an effort to retain this client?

There would be no violation of the rules of conduct of the Institute involved if you should communicate with the petroleum company and the accounting firm in an effort to retain your client.

3. Several civic luncheon clubs make a practice of having one member sponsor each weekly meeting. Premeeting announcements are usually mimeographed on the letterhead of the firm of the sponsor and mailed in his firm's envelopes. Although occasionally remarks are made about the member in question, these are not in the nature of advertising for his firm. Would it be a violation of the Rules of Professional Conduct for a firm of CPAs to allow its letterheads and envelopes to be used in this manner?

There is no objection to the practice of sending occasional announce-
ments of weekly meetings by a service club on firm stationery.

4. Would widespread distribution of a book outlining the history and accomplishments of an accounting firm by the firm in question be considered a violation of the Rules of Professional Conduct?

Inasmuch as distribution of the book in question was limited to one each for all of the officers and directors of the corporations audited by the accounting firm, all members of partnerships audited by them, individual bankers who were personal acquaintances, lawyers with whom partners of the accounting firm were acquainted or had worked with on accounting engagements, and to personal friends of the partners, the committee believes that the method used in distribution of the book was proper.

5. Would the following procedure be considered an ethical practice under the Institute by-laws and Rules of Professional Conduct?

A trade association has requested several accountants to join with the association in distributing profit-and-loss percentages to all of its members. These percentages would be taken from the reports of the accountants' clients and mailed to every member of the industry by the association, indicating that the figures are submitted through the courtesy of "John Jones, Robert Brown, and so forth, CPAs." The information would go to members of the association whose accountants are not in this special group.

There would be no violation of the rules of conduct in the proposed procedure, provided the accounting firms involved have permission from their own clients to compile and distribute the figures in question. It might be more appropriate to indicate that the information is submitted with the permission of the clients of the certified public accountants, rather than through the courtesy of the CPAs.

Rule 9

I have been approached by an attorney to perform some accounting services in connection with a trade-mark infringement damage suit. A fee based on a percentage of the damages collected is proposed. Does this violate Rule 9 of the Rules of Professional Conduct?

The suggested fee arrangement based on a percentage of the damages collected, for accounting services performed in connection with a trade-mark infringement damage suit, would be a violation of Rule 9 of the Rules of Professional Conduct. Such an arrangement would not appear to fall within the exception covered by the last sentence of Rule 9.

Rule 10

1. I have recently moved to another building and the management has suggested that I attach a bronze plaque to the outside wall of the building, containing my name, title, and room number. Would this violate
any of the rules of conduct?

There would be no objection to the plaque proposed, so long as it is modest in size and not in such a form as to be considered advertising.

2. The local radio station last night broadcast a lengthy advertisement concerning a new tax book written by a member of the Institute. Do the Rules of Professional Conduct allow radio campaigns of this type?

Advertisement of a book written by a member of the Institute has not been held to be a violation of the Rules of Professional Conduct of the Institute. The rules prohibit advertisement of the professional attainments or services of a member. If a member is the author of a book, however, the advertising is done by his publishers, not by himself, and there seems nothing improper in reference to the author’s professional qualifications.

3. Would there be any violation of the Rules of Professional Conduct if I supplied to the local bar association, which is conducting a course of tax education, a master tax guide bearing my name as a practicing certified public accountant on the cover?

Distribution of such a pamphlet among lawyers with whom you had no personal acquaintance would be regarded as advertising within the meaning of Rule 10. In the circumstances you describe, the material could be provided without your name imprinted on the cover, without any disadvantage to those who would make use of it.

4. Would there be any impropriety in a member having his name and the words “Certified Public Accountant” or “Public Accountant” imprinted on his checks?

There is no objection to the use of either designation on checks by practicing accountants inasmuch as they go only to persons with whom the accountant has had some business relationship.

5. Is there any violation of the Rules of Professional Conduct if a member frequently advertises in the daily press for staff personnel?

Such advertisements are not a violation of Rule 10 of the Rules of Professional Conduct. This rule does not cover advertisements for personnel, but specifically refers to advertisements of “professional attainments, or services.”

**Rule 10(b)**

Would it be permissible to list in small type in future issues of the classified telephone directory the names of the certified public accountants on our staff, with the firm name and business address?

To list in a classified telephone directory in addition to the name and
address of the firm, the names of the certified employees followed by the firm name and address, would be contrary to Rule 10. Presumably the firm would pay for the supplemental listings. The repetition of the firm name, even if scattered throughout the list, would constitute display with the effect of advertising.

Rule 13

1. A and B are partners in the practice of public accounting. An enterprise in which A has a 19 per cent interest will require an examination in the near future, such report to be furnished to banks, credit agencies, and vendors. Can B make an examination (without using the partnership personnel or facilities) of this enterprise in which A has an interest and render an independent opinion without disclosure of B's affiliation with A in a public accounting practice?

In the opinion of the committee, accountant B could not make an examination of an enterprise in which his partner A has a 19 per cent interest, and be in a position to render an independent opinion, without disclosure of B's affiliation with A as partners in public accounting practice. If the enterprise is financed through the public distribution of securities, B as a partner of A might be precluded from furnishing an opinion on the financial statements under the provisions of Rule 13 of the Rules of Professional Conduct.

2. We have been engaged to audit a partnership, one of the members of which is a brother-in-law of one of the partners of our accounting firm. In addition, the client's office manager is a brother of this partner in our accounting firm. Should disclosure of this relationship be made in our report? We also are to audit a corporation in which this brother-in-law is a minority stockholder.

In the light of the obvious purpose of Rule 13 of the Rules of Professional Conduct of the Institute, it would be most desirable for you to disclose the relationships mentioned in your reports on the audits of the enterprises concerned. A simple statement in your report to the effect that Mr. X, partner of your firm, is related to the individuals who occupy important positions or hold stock, as the case may be, in the clients concerned should be sufficient.

3. Another member of the Institute and I propose to form a partnership for the practice of public accounting. Both of us are members of the Institute. My proposed partner is and will remain controller of a client of mine. It will be distinctly agreed that this client will be serviced from my office in another state and that my partner will have no interest directly or indirectly in the services rendered by me to the client, its subsidiaries, or related interests, or to any employees or stockholders of said client, its subsidiaries, or related organizations. Before entering into such a partnership, I should like to get your opinion as to whether such
a relationship would be contrary or may be considered improper under the Rules of Professional Conduct.

You would be wise to avoid the arrangement through which you would enter into a partnership with another member of the Institute while such member was serving as controller of a client-company, unless you were willing to give up the audit of the client-company.

**Rule 16**

*Is the purchaser of an entire practice or certain accounts of the seller practitioner entitled to receive working papers, copies of income tax returns, correspondence, and so forth, pertaining to the accounts being sold? Is it possible to transfer such vital data without violating the confidential relationship of the practitioner and his clients?*

In no event has the practitioner who sells an accounting practice the right to transfer working papers, and so forth, of a client without first obtaining his permission to do so.

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**Appendix B**

**INSTITUTE BY-LAWS AND RULES**

The following are excerpts from the Institute's by-law provisions concerning discipline:

**Article V, Sections 4 and 5**

Section 4. A member renders himself liable to expulsion or suspension by the trial board if

a. he refuses or neglects to give effect to any decision of the Institute or of the council, or
b. he infringes any of these by-laws or any of the Rules of Professional Conduct as approved by the council of the Institute, or
c. he is declared by a court of competent jurisdiction to have committed any fraud, or
d. he is held by the trial board to have been guilty of an act discreditable to the profession, or
e. he is declared by any competent court to be insane or otherwise incompetent, or
f. his certificate as a certified public accountant is revoked or withdrawn by the authority of any state, territory, or territorial possession of the United States or of the District of Columbia, or
g. his certificate as a certified public accountant shall have been revoked or withdrawn by the authority of any state, territory, or territorial possession of the United States or of the District of Columbia and such revocation or withdrawal remains in effect.
Section 5. A member shall be expelled if the trial board finds by a majority vote of the members present and entitled to vote that he has been convicted of a felony or other crime or misdemeanor involving moral turpitude. If in such case the conviction shall be reversed by a higher court, such member may request reinstatement and such request shall be referred to the committee on professional ethics which, after investigating all related circumstances, shall report the matter to the trial board, with the committee’s recommendation, whereupon the trial board may, by a majority vote of the members present and entitled to vote, reinstate said member.

**Article VI, Sections 1, 2, 3, 4**

**Trials and Penalties**

Section 1. Any complaint preferred against a member under Section 4 of Article V shall be submitted to the committee on professional ethics. If, upon consideration of a complaint, it appears to the committee that a prima facie case is established showing a violation of any by-law or rule of conduct of the Institute or conduct discreditable to a public accountant, the committee on professional ethics shall report the matter to the executive committee, which shall summon the member involved thereby to appear in answer at the next meeting of the trial board.

Section 2. If the committee on professional ethics shall dismiss any complaint preferred against a member, or shall fail to act thereon within ninety days after such complaint is presented to it in writing, the member preferring the complaint may present the complaint in writing to the trial board.

The trial board shall make such investigation of the matter as it may deem necessary and shall either dismiss the complaint or refer it to the executive committee, which shall summon the member involved thereby to appear in answer at the next meeting of the trial board.

Section 3. For the purposes of adjudicating charges against members of the Institute as provided in the foregoing sections, the executive committee shall instruct the secretary to send due notice to the parties concerned at least thirty days prior to the proposed session. After hearing the evidence presented by the committee on professional ethics or other complainant and by the defense, the trial board by a majority vote of the members present and voting may admonish or suspend for a period of not more than two years the member against whom complaint is made, or by a two-thirds vote of the members present and voting may expel the member against whom complaint is made. The trial board shall decide, by majority vote of the members present and voting, whether the statement to be published shall disclose the name of the member involved. A statement of the case and the decision of the trial board thereon shall be prepared by a member or members of the trial board, under a procedure to be established by it, and the statement
and decision as released by the trial board shall be published in *The CPA*.

Section 4. At any time after the publication in *The CPA* of a statement of the case and decision, the trial board may, by a two-thirds vote of the members present and voting, recall, rescind, or modify such expulsion or suspension, a statement of such action to be published in *The CPA*.

**Article IX, Sections 2(a) and (c)**

Section 2. a. The council shall elect from its present and former members a trial board of twenty-one members to be first created by electing seven members for a term of one year, seven members for a term of two years and seven members for a term of three years. Thereafter, beginning with the second year of the trial board's existence seven new members shall be elected each year to serve for a term of three years. Vacancies shall be filled by the council for the unexpired term. No member of the committee on professional ethics shall be a member of the trial board. A quorum shall consist of fifteen members.

c. The committee on professional ethics shall be elected by the council and shall consist of five members of the council not members of the executive committee.

**Article X, Section 3**

Section 3. The committee on professional ethics shall perform the duties set forth in Section 1 of Article VI and may advise anyone applying to it as to whether or not a submitted action or state of facts warrants a complaint against a member of the Institute, provided, however, that if the committee finds itself unable to express an opinion, such inability shall not be construed as an endorsement of the action or state of facts.

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**Rules of Professional Conduct**

**American Institute of Accountants**

**As Revised December 19, 1950**

(These rules of conduct supplement the disciplinary clauses of the By-Laws.)

1. A firm or partnership, all the individual members of which are members of the Institute, may describe itself as "Members of the American Institute of Accountants," but a firm or partnership, not all the individual members of which are members of the Institute, or an individual practicing under a style denoting a partnership when in fact there be no partner or partners, or a corporation, or an individual or individuals practicing under a style denoting a corporate organization shall not use the designation "Members of the American Institute of Accountants."

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2. A member shall not allow any person to practice in his name who is not in partnership with him or in his employ.

3. Commissions, brokerage, or other participation in the fees or profits of professional work shall not be allowed directly or indirectly to the laity by a member.

Commissions, brokerage, or other participation in the fees, charges, or profits of work recommended or turned over to the laity as incident to services for clients shall not be accepted directly or indirectly by a member.

4. A member shall not engage in any business or occupation conjointly with that of a public accountant, which is incompatible or inconsistent therewith.

5. In expressing an opinion on representations in financial statements which he has examined, a member may 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 statement; or
c. he is materially 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 generally accepted accounting principles or to disclose any material omission of generally accepted auditing procedure applicable in the circumstances.

6. A member shall not sign a report purporting to express his opinion as the result of examination of financial statements unless they have been examined by him, a member or an employee of his firm, a member of the Institute, a member of a similar association in a foreign country, or a certified public accountant of a state or territory of the United States or the District of Columbia.

7. A member 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 may furnish service to those who request it.

8. Direct or indirect offer of employment shall not be made by a member to an employee of another public accountant without first informing such accountant. This rule shall not be construed so as to inhibit negotiations with anyone who of his own initiative or in response to public advertisement shall apply to a member for employment.

9. Professional service shall not be rendered or offered for a fee which shall be contingent upon the findings or results of such service. This rule
does not apply to cases involving Federal, state, or other taxes, in which the findings are those of the tax authorities and not those of the accountant. 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.

10. A member shall not advertise his professional attainments or services:

a. The publication of what is technically known as a card is restricted to an announcement of the name, title (member of the American Institute of Accountants, CPA, or other professional affiliation or designation), class or service, and address of the person or firm, issued in connection with the announcement of change of address or personnel of firm, and shall not exceed two columns in width and three inches in depth if appearing in a newspaper, and not exceed one-quarter of a page if appearing in a magazine or similar publication.

b. A paid listing in a directory is restricted to the name, title, class of service, address and telephone number of the person or firm, and it shall not appear in bold type, box, or other form of display, or in a style which differentiates it from other listings in the same directory.

11. A member shall not be an officer, director, stockholder, representative, or agent of any corporation engaged in the practice of public accounting in any state or territory of the United States or the District of Columbia.

12. A member shall not permit his name to be used in conjunction with an estimate of earnings contingent upon future transactions in a manner which may lead to the belief that the member vouches for the accuracy of the forecast.

13. A member shall not express his opinion on financial statements of any enterprise financed in whole or in part by public distribution of securities, if he owns or is committed to acquire a financial interest in the enterprise which is substantial either in relation to its capital or to his own personal fortune, or if a member of his immediate family owns or is committed to acquire a substantial interest in the enterprise. A member shall not express his opinion on financial statements which are used as a basis of credit if he owns or is committed to acquire a financial interest in the enterprise which is substantial either in relation to its capital or to his own personal fortune or if a member of his immediate family owns or is committed to acquire a substantial interest in the enterprise, unless in his report he discloses such interest.

14. A member shall not make a competitive bid for professional engagement in any state, territory, or the District of Columbia, if such a bid would constitute a violation of any rule of the recognized society of certified public accountants or the official board of accountancy in that state, territory, or district.

15. A member of the American Institute of Accountants engaged in an
occupation in which he renders services of a type commonly rendered by public accountants, must observe the by-laws and Rules of Professional Conduct of the Institute in the conduct of that occupation.

16. A member shall not violate the confidential relationship between himself and his client.

Appendix C

SELECTED BIBLIOGRAPHY


"Ethical Problems of Modern Accountancy," Vawter Foundation Lectures, Northwestern University, 1932, Ronald Press, New York, 1933. (Accountancy as a Profession; The Accountant and the Investor; The Accountant and the Stock Exchange; The Accountant and his Clientele; the Accountant and the Investment Banker; The Accountant and his Profession.)


