Woman C.P.A.

Volume 25 | Issue 3 Article 1

4-1963

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It has become almost a cliché to say that the world is divided into opposing camps. Yet as in the case of most clichés, there is a high degree of truth in this statement. Yes, today the world is divided into opposing camps, not only in terms of political philosophy which results in different forms of government, but also in the alternative economic systems applied. The vital overall objective of every society, however, must be to assure economic growth and higher standards of living, regardless of the economic system adopted.

In their attempt to achieve this goal, nations can no longer isolate themselves, but must draw on the resources of others, resulting in international trade and flow of capital between the nations. The market where international demand and supply meets is an extremely competitive one, where price is the all-powerful factor enforcing the most effective utilization of the international resources.

In economies, based upon a free enterprise system without a central agency to govern or to direct economic activities of the individuals, decisions as to what to produce, when to produce and what methods and resources to use, are completely at the discretion of each entrepreneur. Such decisions and the resulting success or failure affect, not only the individual concerned but the societies as a whole. Every erroneous decision results not only in financial loss for the individual but also in waste of national resources thereby jeopardizing the overall objective of continuing growth.

It is obvious that entrepreneurs faced continuously with such vital decisions need a dependable device capable of assisting them in gathering facts and testimony necessary for reaching conclusions and transforming these conclusions into well informed decisions. They need a device which furnishes quantitative data that can be used as a basis for making the necessary choices among the available alternatives and which can be used for checking and evaluating progress and results. Such dependable device is also necessary for appraising the overall performance of free enterprise systems.

The forceful instrument available for organizing, expressing and evaluating business and economic facts is accounting. Accounting is not only the universal language for thinking and communicating about business and economic affairs, it is also the quantitative mean for disclosure of information essential to the successful conduct of national and international market economies and for appraising the overall performance of free enterprise societies. As the best available device for understanding today's complex business transactions and their interrelationships, accounting has become accepted as the most nearly ideal tool for measuring the performance of individual economic units or enterprises.

Dr. Ramanauskas discusses Accounting and World Economy at one of the simultaneous technical sessions at the Eighth International Congress of Accountants, held last September in New York.

In a dynamic free enterprise system, every business enterprise in its struggle to maintain its existence in highly competitive and rapidly changing national and international markets, has to make intensive use of the special information service provided by enterprise accounting. Over the centuries, enterprise accounting has developed from the simple financial information aid for owner-operators of business enterprises into a complex instrument, capable of furnishing not only periodic financial information but also providing important aid to the internal control and management of mammoth corporations engaged in mass production at high levels of output, competing in national and international markets. This development necessitated a modifying and refining of the accounting tools, originally constructed for periodic financial reporting only, into multipurpose tools capable of dealing with profit reporting as well as with cost and output control in an efficient and stimulating way. This process of broadened accounting thinking and application is still in flow because steady social and economic changes of todays dynamic economies require continued reorientation in existing modes of accounting thinking.

Why do business enterprises of today need such a multipurpose tool and can no longer manage with a tool capable of periodic income reporting only?

The all powerful factor controlling the enterprises's activities in our modern societies is the price, the price which can be realized for the finished products and the price which must be paid for all the factors necessary for their production. The margin between must be such that the existence of the enterprise is justified. In other words, it must be sufficient to enable the producer not only to maintain the enterprise's substance, but also to accumulate sufficient funds for its organic growth and to provide a satisfactory return for the investors. Price is the factor which influences each firm's activities and its decisions with regard to production and distribution. The businessman attempting to distribute his products in highly competitive markets, must keep his prices low enough to compete successfully and not price himself out of the existence. Only then will he have an opportunity to yield a profit if he is able to keep his costs sufficiently below their related revenues.

In the international market and in foreign competition in the domestic market, an American entrepreneur is additionally handicapped. He must compete with American companies operating under similar cost structures, and also with foreign companies having the advantage of a significantly lower wage level. Since a decrease in American wages rates is neither possible nor desirable, successful competition depends upon management's ability to obtain the highest degree of efficiency in labor and other cost factors. This increased efficiency is particularly important if we are to operate successfully under a common market system.

It is therefore obvious that with industries operating at high levels of output and distributing in highly competitive markets, cost planning, their control and reduction are the most problematic and vital tasks of modern enterprise management since upon their success or failure depends the future of the enterprise and the prosperity of the economy as a whole.

Because of the aforementioned circumstances, it is no surprise that the process of modifying and refining traditional tools and procedures advanced particularly in the field of cost accounting. Successful attempts were made to overcome the weaknesses in the conventional static reporting methods by incorporating means for measuring performance and by developing attachments in the form of supplementary reports, special analyses and break-even charts. New concepts for income determination and matching costs and revenues were introduced. A complete new method for accounting and controlling costs was developed, which claims to give more meaningful results to management without the necessity of preparing additional time-consuming reports.

This new costing philosophy, commonly known as direct or marginal costing, differs from the so-called orthodox costing methods mainly in that it emphasizes income maximation and not income determination only. In the process of absorbing cost to value inventories and cost of goods sold, the direct costing approach identifies with the product only prime cost (direct labor and direct material) and those manufacturing costs which are conveniently traceable to them, namely their variable portion. All other items of manufacturing costs or their fixed portion are considered to be overall costs of operation in the period of occurrence and are immediately expensed. In establishing their necessary monthly gross margin or spread between direct cost and selling price, management is required to provide for indirect factory expenses (the fixed portion of manufacturing cost) as one of the costs of doing business, as well as with administrative and selling expenses.

The orthodox costing methods disregard the basic knowledge that certain manufacturing overhead costs remain constant regardless of the quantity of products produced, while others will fluctuate with the level of output, just as the prime costs would. Allocation of the total manufacturing overhead to the products produced and sold is accomplished at an estimated rate based on actual or predetermined volume. Since those rates are based on estimates in regard to manufacturing costs as well as quantities of product which would bear such cost, the absorption process must result in over or underabsorption of manufacturing burden whenever actual cost or production volume differs from the estimates. This over or underabsorbed balance must be analyzed as to components or reasons by supplementary reports, if management is to secure some explanation for this symptom of cost-volume-profit relationship.

Nonconventional profit and loss statements prepared under the direct costing approach show the figures free from such influences and enable comparisons of the results of several years or different production levels without the necessity of any additional analysis or explanation.

The vigorous debates over the merits or demerits of this new costing concept vs. the orthodox methods have been going on since

1936 and literature is full of reappraisals of this controversial unsettled issue in the light of today's knowledge of other recent developments. The reason for the continuance of this pro-and-con battle lies in the fact that two groups are involved and that their opposite viewpoints are actually at issue. The managerial segment is interested in tools suitable for short run decisions as to optimum combination of price and output. The accounting theorists and practitioners concentrate on long run objectives of income determination within the framework of generally accepted accounting concepts and principles.

The managerial segment sees in cost accounting not an end in itself, but a means to an end and emphasizes the uses to be made of cost data. They determine how good a specific costing method is, not by reference to a stated body of principles or established concepts, but in terms of how well the method meets their needs. It is true that direct costing by separating costs according to their behavior in regard to volume provides management with an additional tool for achieving better control over expenses. The accounting information provided by this method is more understandable and more useful in arriving at day-to-day decisions.

It is equally true, as advocated by the opposing accounting professionals, that direct costing emphasizes cost control at the cost of the time-honored principle of profit determination. Cost control, however, is only one of the many goals to be accomplished through efficient costing methods and it would not seem justified to emphasize one task at the cost of another. Direct costing, furthermore, violates the generally accepted accounting principle of properly matching cost and revenue, by valuing inventories at direct costs (prime cost and variable portion of manufacturing overhead) only, and by excluding completely and expensing immediately the fixed portion of manufacturing expenses.

Those are the reasons why the direct costing approach has not yet become a generally accepted method for external reporting and income tax purpose, despite the fact that it has been increasingly used in industry.

That direct costing as of today, has not been able to provide management with the multiple purpose tool equally suitable for cost control as well as profit reporting as intended at the outset, seems of secondary importance. The real importance of this new costing philosophy lies in the fact that by focusing attention for the first time on the distinction between variable and fixed cost, it recognizes that costs are influenced by both production and sales volume. Thereby it qualifies as one of the tools of a much broader new development namely, of managerial accounting. The goal of this new branch of accounting is to supply management with sound bases for its decisions as to what to produce, what volume to produce and what prices must be placed on the output to warrant survival in the competitive struggle, organic growth and a satisfactory return for the investors.

The advocators of the absorption cost methods believe that the proper price for any product must permit full recovery of all costs and that enterprises must fail if they disregard this basic truth. This philosophy is certainly true as a long range objective, but management is more interested in short range thinking, because it cannot operate successfully in today's competitive markets by using solely long range static pricing policies. To compete successfully, management is willing to reduce its selling price in order to obtain the business, because the sale would return the variable costs as well as a share of the fixed expenses, thereby making a contribution to the pool of fixed expenses and reducing them by a small amount, which is more desirable than no sale at all. Direct costing supplies management with the tools for this type of short range pricing procedures, often termed marginal income approach because of its differentiation between variable and fixed expenses.

Another indirect accomplishment of the direct costing approach is that it has forced cost accountants to reevaluate thoroughly their conventional methods in the light of changing conditions of the economies of our days, which resulted in the use of attachments as supplementary devices.

Whether these conventional methods assisted by these supplementary devices will still be adequate in the future, whether direct costing or a modification of it will become so popular as to be generally accepted or whether the accounting profession will be forced to develop true multipurpose tools, capable of income reporting as well as profit-volume-cost control is still an undecided issue.

After having evaluated the direct costing approach as to its ability to serve management and as to its qualification for external reporting purpose, let's evaluate in these respects also one of the conventional, generally accepted costing methods, since one of the arguments advanced by critics of direct costing is that the information highlighted by the direct costing approach is also available under the traditional absorption methods.

Are they justified in stating that there is no necessity to change the present philosophy of income reporting and all that is necessary is the proper use of the tools which good accounting and control already provide?

The various historical costing methods used in the past were mainly retrospective cost finding procedures, with severe shortcomings in providing management with information needed for effective cost control. Their most vital shortcoming was the lack of a yardstick to measure performance of men and departments and their use of materials, labor and expenses. Furthermore, the data provided was available only at the end of the accounting periods, thereby preventing management from taking corrective action immediately before a great damage had been done. In today's highly competitive economies, efficient production must be preplanned, and at each stage in the operation of the plan, actual and expected achievements must be compared, taking any necessary remedial action to correct "off the course" tendencies.

In the process of modifying their tools to present-day requirements, the cost accounting segment of the profession developed a new absorption method called standard costing, which makes use of carefully predetermined costs for specific conditions at a stated volume of output. These predetermined standard costs are compared with the actual costs incurred as the work proceeds and the differences between the two, known as "variances" are analyzed by supplementary reports as to causes.

Usually the analysis takes place as part of the ordinary accounting routine and insures not only that regular checks are made upon the actual expenditures incurred, but also their way of presentation enables management to concentrate only upon matters which are not proceeding according to the predetermined plan. This results in reduction of managerial time necessary for the controlling task. If prompt action is taken by management on the lines indicated by the analysis reports, effective cost control and reduction will be secured. Since standards are constantly studied and reevaluated with a view to improvements, control over cost is further facilitated.

Standard costs further assist management's intelligent estimating of profitable selling prices. In order to arrive at expected costs and sales prices it is merely necessary to build up the estimates by changing the established standards to current conditions. Even the marginal income approach for short range income policies will be simplified by using standard costs, especially when such are used in connection with a flexible budget and when the manufacturing expenses are broken down into their variable and fixed elements.

The use of standard costs is possible in all types of business enterprises where the products or their components can be standardized. Its efficient application becomes doubtful if there is such a wide variety of products of a nonstandard nature that the cost of setting standards becomes prohibitive and out of proportion to the value received from their use.

To the limitation in applicability comes as another shortcoming, that the accounting profession has not yet been able to agree upon a uniform method with respect to the disposition of variances. One group believes that standard costs represent the true costs and any variance is not an increase or decrease in manufacturing costs, but rather a deviation from contemplated costs caused by vicissitudes of business fortune. The advocates of this viewpoint charge or credit to income or expense all deviations from standard at the end of the accounting period, thereby showing ending inventories, as well as cost of goods sold, at standards for external reporting purpose.

Another group of accountants considers actual cost as true cost and prorates all variances between cost of goods sold and inventories (work in process and finished goods) thereby converting the figures for reporting purpose back to actual. The portion of variances applicable to the inventories is thus fully deferred, which results in a higher profit figure for the current period. This second viewpoint seems justified only if the standards were not changed for a considerable length of time and needed a revision.

A third group, taking a middle ground, holds that quantity variances caused by inactivity, waste or extravagance should be written off, but price and budget variances should be deferred and charged to an inventory reserve account to an extent which would bring the inventories up to current values. Any excessive price and budget variances are written off as excess costs. Under this most broadly accepted method, the inventories are on the books valued at standard, while for reporting purpose, by the use of the inventory reserve, they are stated at approximately current market values. Losses caused by excessive costs, and inefficiencies are charged to the current periods. Gains resulting from excess capacity or extreme efficiency are accounted for in the period they occur.

A further weakness of standard costing lies in the fact that even if used in connection with a flexible budget and expenses segregated into fixed and variable components, the volume variances cannot be avoided completely as long as actual and estimated production differs.

The discussions so far have shown that standard cost certainly constitutes a vital step forward in securing real managerial value from cost accounting procedures. Its forward looking approach to all functions insures the most effective use of material, machines and services. Management is able to see what should happen and hence can make confident forecasts with regard to future costs and profits. Prices can be based on well informed estimates. Inefficiencies are promptly revealed, thus maintaining profit expectations set by budgets. However, this system is not capable of eliminating the symptoms of the cost-volume-profit relationship completely and requires supplementary explanatory analyses to qualify as a cost control device instead of a mere cost finding procedure.

After having analyzed some progress in broadened accounting thinking in the specialized field of cost accounting, let's examine the present stand in modification of basic general accounting principles and postulates. Are they capable to function effectively in this complex and expanding world of our days? The literature of the past years was filled with appeals for recognition of the critical fact that basic accounting philosophies suffer from obsolescence and that there exists an urgent need for close reexamination of many of our accounting concepts, basic postulates and procedures in terms of economic, social and institutional conditions that prevail today.

In accomplishing the task of meeting new situations, our discipline relied upon tradition, quite in contrast to physical sciences and other areas of knowledge where reliance is placed upon past ideas only if they can be proved anew. In other words, the researcher in physical science does not accept anything from the past as authoritative unless he is capable of proving it in the present. Past acceptability and usage, in other words, tradition, has no weight in those fields of knowledge. Each new problem is approached through objective research, independent or empirical studies.

In accounting, reliance grew only from the fact that an idea had been widely used. After ideas or practices became generally accepted, they were used again and again without reevaluation as to their merits and justifications under current conditions. This continued utilization of ideas and practices with little or no conscious reference to their present merit and validity of their basic premises, but with past usage as the only justification for continuation, was a severe handicap in the process of broadening and modifying accounting thinking, since it hindered the development of new ideas which lacked the advantage of being tried and true.

Not all knowledge and techniques from the past deserve discrediting simply by attaching the detrimental connotation of "tradition" to them. However, the fact that they are not always the answer to present situations needs broader recognition. Not their age, but their failure to meet the test of present soundness and usefulness, is the reason for their necessary replacement by newer approaches in closer accord with existing circumstances.

In the process of advancing knowledge and obtaining solutions to practical everyday problems, the shocking discovery was made that our discipline lacks a basic theoretical frame of reference or a set of objective basic premises on which all accounting theories can be based, and against which they can be tested for validity. In other words, the superstructure of accounting theory rests on a rather shaky foundation, a foundation which is not qualifying our discipline as a science, which according to Plato should be based on a system where all the asserted propositions which are not self evident, should be based on those which are.

This lack of a coordinated system of postulates principles and rules was caused by the fact that in the past research was done mainly with the goal of obtaining solutions to practical everyday problems. Very little fundamental or constructive research was done; research which was not hampered by considerations of immediate practical use, but which applied the attitude of natural sciences to the subject matter.

To overcome this severe weakness in our discipline, the American Institute of Certified Public Accountants founded an Accounting Principles Board which was given the task to establish, through constructive research, basic premises or postulates upon which all accounting theories or principles are to be based.

This vital undertaking of the profession is one of the most revolutionary steps in accounting history and places the discipline on the threshold of a true science. On the success or failure of this undertaking will depend whether or not our discipline shall have for the first time something other than general acceptance as a standard to measure merit or demerit of accounting principles or practices. If the experts in our field are successful in developing irreducible postulates, broad and objective enough to serve as solid structure for the formulation of principles and the development of a well coordinated set of rules for application in specific situations, the historical, pragmatic approach could be replaced and the advancement of our discipline to a scientific status seems assured.

The first research results are now published. However, as it was to be expected, much additional thinking and creative work will be necessary before they will be crystalized into a body acceptable as solid structure of a discipline attempting scientific status.

On The Twenty-Fifth Anniversary Ida Broo Looks At ASWA.

What are my thoughts looking back over the 25 years of membership in the American Society of Women Accountants and at the same time looking to the future? Has the organization made satisfactory progress in realizing its initial purposes, which were: To improve the efficiency of its members in their profession; to further the opportunities in the profession for women; and to establish a good fellowship among members of the accounting profession?

As you are aware, the American Society of Women Accountants was organized by the American Woman's Society of Certified Public Accountants because it was felt that lack of opportunity rather than lack of ability prevented women from being substantially represented in the accounting profession. In 1937 there were but 130 women certified public accountants in the United States. With the population at that time standing at 130 million, this represented one in a million. Since then the number of women who acquired certificates has increased ten fold.

The American Society of Women Accountants is broader in scope than its parent organization because it admits to membership women not certified but employed in accounting, teachers of accounting and advanced students of the profession. The Indianapolis Chapter was chartered in 1938 with three members. Today there are 75 chapters with over 3500 members.

Through chapter programs, regional and national meetings, members have opportunities for exchanging ideas, for keeping current on professional developments as well as enjoying fellowship with other career women. Two regional meetings in the immediate future are scheduled for Indianapolis, May 16-19, and Sacramento, June 14-16. I would like to extend my personal invitation to celebrate our 25th anniversary at Indianapolis. Please try to be there.

Sincerely,

Ida S. Broo, Founding President

Their main shortcoming seems to be that they are still too narrow and conservative. To serve as a sound foundation, the body of prospective postulates must be broad and general, international in character, although developed principles and practices may be subject to modifications in view of specific situations existing in different parts of the world. The search for postulates must also extend into the boundaries of the field and must take into consideration that accounting is not only affected by social and economic conditions, but also affects actions in various fields through its results because of its coextension with all human action in its economical aspects.

Because of the necessity of a uniform international approach there seems to exist an urgent need for a more permanent form of international association of the accounting professionals of the world, such as this periodic international congress provides. What is needed is a permanent international forum of some sort, where professionals and theorists of our discipline could exchange new ideas, criticize and modify old ones and where they can participate in the present evolutionary undertaking of crystalizing a sound framework of international postulates and principles.

A vital demand also seems to exist for an international publication, where articles of broad interest are translated and published in the major languages to enable world wide interchange of ideas, experiences and inspiration by accounting professionals without the necessity of time-consuming search and interpretations by each.

Such a combined effort could accelerate tremendously the present constructive research task and could assure international uniformity and future progress.

The time has come where accounting, the most dependable quantitative device for measuring and appraising performance and progress of individual business units as well as whole economies, is faced with its greatest challenge ever encountered. A challenge where it has not only to prove that it is capable of providing accommodations for financial reporting and controlling which are in harmony with the requirements of the rapid developing and changing economies of our days, but where it has also to prove that it has reached the maturity of a true science. Let's make this transformation process an international effort and success.