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The Accountant's Function as Business Advisor *

BY ARTHUR ANDERSEN

The time when the accountant was viewed by business men as a necessary evil is not entirely past. Yet it is true that in the last decade business men have learned that the accountant is more than a compiler of figures and a detector of defalcations. In the experience of the past ten years the business man has found that advice from an accounting viewpoint may have a high cash value in the form of taxes saved or refunded, war contracts liquidated, in recapitalizations and refinancings effected advantageously. These tangible "money" results the business man can recognize as constructive work—which is entirely natural, since the final analysis of his own business lies in the figures reflected in balance-sheet and income account.

Having arrived at the point where he admits the tangible worth of some phases of accounting effort and advice, the business man is predisposed to study, as having a constructive value, some phases of accounting work to which he has hitherto not given even a serious thought. This is true in the detailed as well as in the broad phases of accounting service. The present-day accountant who is alert will grasp every opportunity to foster this attitude by increasing the constructive value of all normal work and seeking newer and broader fields of service to business management.

CONSTRUCTIVE FEATURES OF AUDIT WORK

The public accountant has an opportunity for direct service to management even in so routine a procedure as the annual audit. The average business executive has no real conception of what an audit is. To him an audit is an "audit." A "balance-sheet audit" and a "detailed audit" are merely technical names to him. And many accountants fail in their duty by not spending the time, effort and thought necessary to make sure that the chief executives clearly understand the scope of work covered, the reasons therefor and the results accomplished. The executive is prone to assume that an audit includes a complete check and verification of the entire accounting transactions during the period covered.

*An address delivered at a regional meeting of the American Institute of Accountants, Chicago, Illinois, November 17, 1925.

In addition to educating management to the real scope and meaning of audit work, the accountant should take every opportunity to improve the working methods of the company's own organization. The methods of internal check should be subject to as close scrutiny as are its results. Weaknesses in internal check should be discussed with the management at the time of the audit and all recommendations made a matter of record in the audit report. Internal check is only one phase to be considered, however. The tangible advantages of clean-cut accounting methods as applied to receivables, payables, credits, order procedures, perpetual inventories, etc., should receive equal emphasis. Personal reductions effected either through revisions of method or the use of machines will be reflected in tangible savings. Provision for the summarization and interpretation of operating results through the proper form of executive reports furnishes the accountant with another opportunity for service.

These constructive contracts are natural outgrowths of audit work, but can be realized only if the accountant has more than an auditing vision and feels the responsibility for constructive service to management.

ADVISORY RELATIONS WITH MANAGEMENT

The service which may be rendered from this somewhat detailed internal viewpoint is only one small sector of the coming field of the accountant. The accountant may aspire to a field of business vision which is almost broader than that held by management itself. The possibilities in this direction have been indicated in the recent past in matters of refinancing and reorganization.

In the past quarter-century business has been forced into a new era of operations. The scope of distribution has broadened, the size of businesses has increased and there have been vertical and horizontal integrations of astounding size. Moreover, increasingly greater amounts of capital have been required and have been provided through the agencies of banks and investment bankers, involving new financial relationships and obligations. Questions of funded, paid-in and temporary capital and their interrelationships have arisen which were previously unknown.

The accountant has had a large place in the consummation of these financings. The actual audit work has been only one of

his responsibilities. Representing the banker, he has needed more than a banking viewpoint, since he has been charged with formulating conclusions as to the operating, merchandising and organization possibilities of the proposed mergers or consolidations. This step beyond the audit which has involved broad and practical analyses of these situations has come to be known as the "financial and industrial investigation" and the results of these investigations have often been far-reaching in their effect. No policies, changes or recommendations can be suggested which are permanently advantageous from the investment-banker's viewpoint unless they are truly beneficial to the business as an operating organization. In the long run, no steps can be taken to protect senior securities unless they consider the interests of junior securities as well. The accountant must therefore have a complete understanding of the viewpoints of both bankers and management. He therefore has come to have an advisory relationship with management which sometimes has been attained independent of immediate financing and which often extends past the first contacts made at the time the consolidation was being effected. His field of consulting relationship may embrace problems involving freights, international credits and exchange, foreign agencies, branch-house control, sales budgets, national advertising, tariffs, patents, plant location, merchandising policies, operating controls, etc.

SCOPE OF ANALYSIS

In filling the function of advisor or consultant to management the accountant is thus entering fields of investigative work which mark a distinct advance over the earlier conceptions of the scope of his service, and which deal with the broad aspects of business as a whole. One of the principal subjects of study is the personnel of the company and the functioning of this personnel as a unified organization. First, the organization plan must be studied; then each man in any position of importance must be studied in the light of his effectiveness in the particular function. These functional standards are naturally flexible and somewhat indefinite, being set as the result of experience and by the results shown. This study of personnel is only one of the elements included under this type of business analysis. There is also the examination of balance-sheets and earnings statements from the business

as distinguished from the theoretical accounting viewpoint. The total of the inventories is less important than the relationship between inventory and sales, or inventory and receivables, or inventory and fixed assets. The current assets may be important by reason of their make-up rather than their value, or by reason of their relationship to current liabilities or to bank loans. The ratio of contributive capital to loan capital is important. The make-up of net worth is far more vital than its amount. The trend of earnings is more significant even than their relation to net worth, which is in turn more important than their actual amount. Earnings in certain years, such as 1921 and 1922, are extremely significant, as furnishing an indication of the soundness and stability of the enterprise.

In the analysis, the geographical distribution of sales may possess great significance as bearing on the future trend of total sales, while the distribution by principal customers may indicate a potentially dangerous condition. The position enjoyed by the company in its own field of industry and the position of the type of business with reference to industry as a whole are also to be considered.

A business analysis of this character embraces also many special side investigations which ordinarily have no place in the work incident to the preparation of audited financial statements. In this class may be mentioned analysis of the distribution of stock-holdings; the make-up of the board of directors (with even the personnel analyses of these directors); studies of the variations in stock control or voting trusts over a period of years; the investigation of principal executives as to age, length of service, salaries, stock interest, prior working experience, etc. These matters usually receive consideration only when the matter of refinancing is involved, but here they may attain a vital importance. The financing may practically hinge upon the question of extent of stock interest by the president or general manager; and a study of salary range and scale may reveal a poorly balanced executive organization.

REALIZING THE FUNCTION AS ADVISOR

The abilities required for analysis must be supplemented by the ability to draw conclusions which will be sound and constructive. This means that the accountant of the future will possess not only a logical mentality and a broad viewpoint fortified by

varied experience, but also resolution and decision. Possessed of these qualities and abilities, the accountant of today will find that he can scarcely avoid the rôle of business advisor. Bankers, on one hand, will seek his outside view on matters of financing, and management, on the other hand, will consult him regarding the best interests of the business.

It is in bringing a balanced view to bear upon the problems of the undertaking and in assisting management in matters of business analysis that the accountant will have his greatest opportunities for service. The public and the commercial accountant must keep pace with the large developments in business. Their viewpoints must be beyond the mere gathering or checking of figures. They must understand more than the pure technique of accounts. The thoroughly trained accountant of the future must have a sound understanding of the principles of economics, of finance and of organization, which are the three fundamental factors underlying any successful business. It is in recognition of these necessities that George F. Baker has been led to endow the Harvard graduate school in the sum of \$5,000,000.

Public accounting as a lifetime profession can not, of course, care for all the men who enter that profession. Some will qualify as partners; more may qualify as managers; but many men will pass through a public-accounting experience to find their real reward in general business. They will become not merely cost accountants, chief accountants, or auditors; they will attain more and more to the top rungs of the ladder and will be charged with broader and more diverse responsibilities, because they have had the training and experience which gives them a true perspective and understanding of the science of business. Where the public accountant may be called upon to investigate, analyze and advise, it is axiomatic that the commercial accountant—the comptroller—must accept the same scope, viewpoints and responsibilities in the service of the management.

In closing, let me leave you with this thought in mind. The acceptance and adoption of new ideas does not necessarily mean progress nor does holding fast to the old always mean conservatism; it may mean stagnation. It is my profound conviction that the accountant of the future will prosper and consolidate his position in the business world in proportion to his breadth of vision and willingness to accept these responsibilities of larger service to industry.