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The Woman CPA

JULY, 1979 VOLUME 41, NUMBER 3

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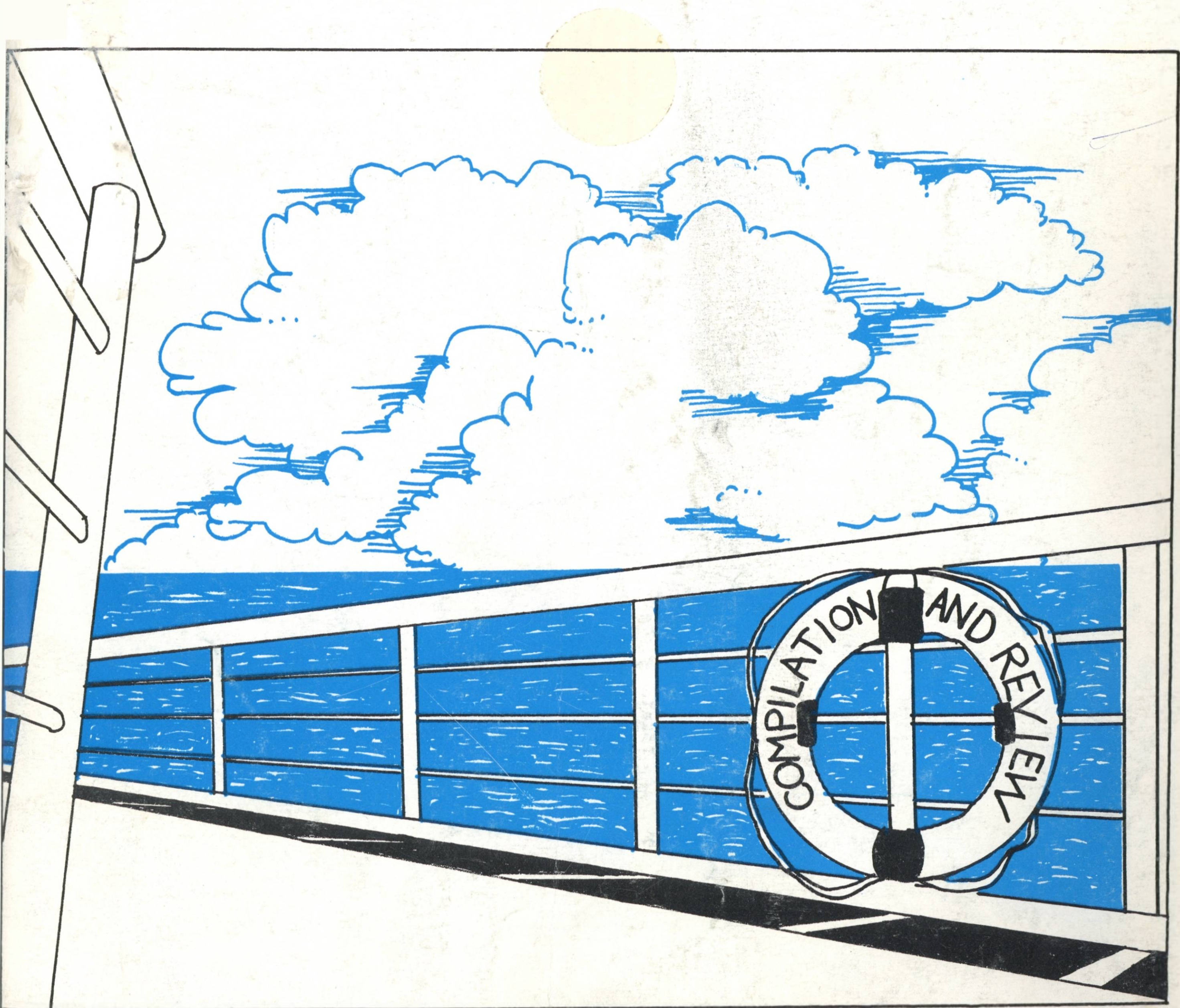

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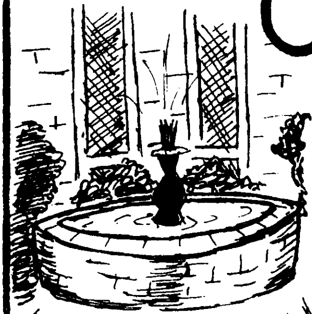

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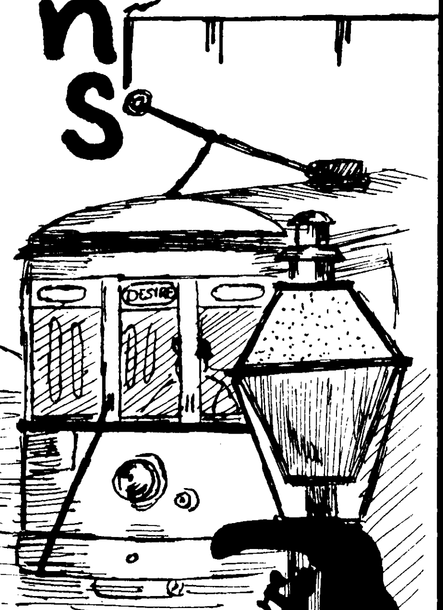

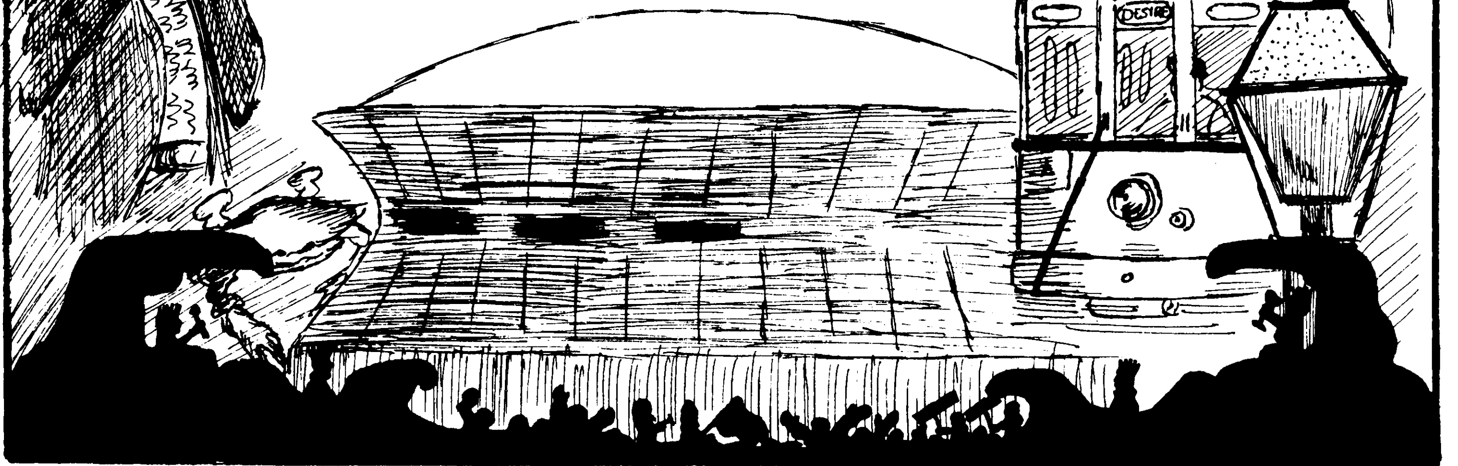

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Editor's Notes

Precise stargazing, and the imperfect art of accounting

From atop the second highest peak of the Santa Rita Range which lifts through Arizona near the Mexican border six mirrors will point into the deep skies tonight and, if the night is clear, each of the six mirrors will reflect its separate image of the chosen star. Celestial twinkling caught by the mirrors of the new Mt. Hopkins telescope will be focused from each of the six reflections into a single image through an electronic control system that uses smaller movable mirrors, lasers, and on-line computers. The compound eye of the MMT, or Multiple Mirror Telescope, is an ingenious method of looking at an object that is too distant to be seen by one large telescope, or at least by a telescope whose enormous lens weighs so much that one additional inch of diameter would cause it to fall in upon itself of its own weight. Multiple mirrors enlarged the reflecting field but presented problems of realignment whenever the telescope changed position, or when heat variations within the observing chamber caused minute changes in the mounting angles. The MMT became a practical instrument only after development of a sophisticated guidance system that realigns each of the artificial star reflections into one common focus.

Can any committee of six persons focus six impressions of a problem into one clear image? When replacement, or current, cost is endorsed for supplemental financial statements by some industries, while others prefer constant dollar reporting, can any common procedure evolve for banking, the forest products industry, insurance, mining, oil and gas, and real estate interests?

It comes to mind that the accounting profession whose problems, unfortunately, are neither distant or obscure, would be marvelously advantaged by a device that could align separate points of view into one indisputable picture. There is no denying that well tempered judgment, however deliberate, is better than the pragmatism of the despot, or the tunnel vision of the fanatic, but wouldn't it be wonderful if some mental equivalent of movable mirrors, and lasers, and on-line computers could, after all the reasonable discussion is over, collect the cogencies and blend them?

Such is the intent of the Financial Accounting Standards Board, of course, with its composite membership from backgrounds of business, government and accounting. The multiple mirror idea is furthered by the Financial Accounting Standards Advisory Council. Instead of six reflectors like the Mt. Hopkins telescope, the combined vision of Board and Council reflects forty-four points of view but as yet nobody has devised mirror, or laser, or on-line computer to automatically focus that collection of knowledge into an image of common truth.

Visions of activity appropriate to accountants are as myriad as points of light in the Milky Way. Each observer sees the light cluster according to a specific point of observation and according to the degree of acuity available. We have on one hillside, so to speak, the Securities and Exchange Commission reporting every observation in an authoritarian way. From another promontory the accountants themselves describe the view, with some obvious straining for accord. On yet another series of platforms client groups report sightings that can be as far apart as the North Star and Southern Cross. Then from atop Capitol Dome the Congress of the United States makes solemn scrutiny as prelude to magisterial announcement.

To clear some of the haze the profession began, on July 1, to give formal definition to the clientele of the level of accountant assurance for each engagement with non-public companies not requesting audit. Clients are advised of the exact services that will be performed at the compilation, or lower, level and at the higher level known as the review. If definition of compilation and review lacks the sophistication of multiple mirrors and lasers and computers, it compensates with the charm of simplicity. Each party to the accounting engagement will know what the other has in mind. The July issue of The Woman CPA presents two articles relating to this new procedure prescribed by the Accounting and Review Service Committee of the AICPA.

One of the most controversial views of accounting activity concerns management advisory services (MAS), a lucrative field that has become exceedingly attractive. Business has tacitly approved MAS by public accounting firms by placing Arthur Andersen & Co. third from the top in 1978 dollar billings as management consultants. Coopers & Lybrand come next in the billing hierarchy, followed closely by four more Big Eight firms.

Seen from another point of view, when accountants advise management and then audit the fruits of management decision, some independence must be forfeited. The public oversight board of the SEC practice section of AICPA counsels the profession to be very circumspect in MAS activities, while simultaneously demonstrating to clients that potential benefits from MAS can outweigh any impairment of auditor objectivity. Meanwhile Senator Thomas F. Eagleton (D-Mo.) condemns combination of MAS with auditing functions and has reminded the profession that the Metcalf subcommittee's proposals for self-regulation will be reinforced by stronger alternatives if accountants fail to put their house in order. Disparate points of view. In this issue we present a discussion of MAS so that our readers may appraise the controversy.

As Americans we have a cultural inclination to tolerate various viewpoints but as accountants we might, once in a while, yearn to wish upon a star for some ingenious focusing device that would bring the separate sightings into one clear view.

Constance T. Barcelona

Compilation and Review

A New Concept of Accounting Services

By Carol S. DeHaven and Donald L. DeHaven

In the early 1970's, the increasing complexity of financial reporting requirements led many accountants to conclude that separate standards and procedures should be developed for some businesses. The Accounting Standards Division of the American Institute of Certified Public Accountants responded to this concern, in part, by undertaking a study of the application of generally accepted accounting principles to smaller and/or closely-held businesses. Among the recommendations from their study was that the unaudited report, especially the "internal use only" disclaimer, be reconsidered.

The AICPA subsequently established the Accounting and Review Services Committee to reconsider all aspects of AICPA pronouncements regarding a CPA's association with unaudited financial statements. In 1977, the committee was designated a senior technical committee with authority to develop standards of reporting on accounting and review services that a CPA may render in connection with unaudited statements of *nonpublic entities.*[1]

One result of this designation was to structurally divide the authority for standard setting relating to unaudited statements between two committees: the Accounting and Review Services Committee for nonpublic entities and the Auditing Standards Executive Committee for public entities. To achieve this transfer of standard-setting authority, certain portions of Statements on Auditing Standards (SASs) affecting nonpublic entities will be superseded as standards are issued by the Accounting and Review Services Committee.

It should be noted that the authority for establishing accounting principles, including financial statement disclosure requirements, remains with the Financial Accounting Standards Board. The FASB has devoted some attention to the concerns of nonpublic entities, as evidenced by its adoption of FASB No. 21. Statement No. 21 suspends earnings per share and segment information reporting requirements for nonpublic enterprises.

SSARS No. 1

Pronouncements of the Accounting and Review Services Committee are known as Statesments on Standards for Accounting and Review Services, hence the acronym SSARS. The first statement issued by the committee, "Compilation and Review of Financial Statements," is intended to define the types of services possible and related reports that a CPA may render in conjunction with unaudited financial statements. The accompanying article by Carol Hardan, "Compilation and Review: Definitive Services," differentiates types of unaudited services and presents examples of accountants' reports which would result from each. The purpose of this article is to describe some of the factors which should be considered in evaluating and implementing the statement.

It is important to realize from the first that the entire area which was previously referred to as unaudited has been separated into two parts: compilation and review. No longer will a presentation of financial statements be considered as either audited or unaudited; the statements will be either audited, reviewed or compiled. Even so, the term unaudited may continue in use. If it does, it will have meaning in a general sense only and the term itself will no longer appear on the face of the financial statements.

A major part of the impetus for this change in the unaudited area was that, in the past, all unaudited financial statements bore the same disclaimer of opinion regardless of the extent of procedures performed by the CPA. The accountant was not able to issue a report which described the service being performed or any conclusions which had been reached.

SSARS No. 1 provides accountants with a means of communicating more clearly to clients and third-party users the level of assurance, if any, that is expressed on the information in the financial statements.

Levels of Assurance

The lowest level of assurance is that expressed by the compilation report based upon a compilation service. The compilation service relies almost exclusively on source data or summary information from the client. Although the CPA may choose to analyze, verify or corroborate the information received, compilation standards do not require any such procedures. Furthermore, SSARS No. 1 does not permit the CPA to specify in the report whether any procedures were performed. Thus, the standard form of the accountants' report properly contains a warning to the statement reader that no assurance can be expressed on the financial information based on compilation procedures.

In other words, the compilation service consists of presenting information supplied by the client *in the form of* financial statements. Accommodation typing or reproducing of financial information is no longer permitted as the CPA is required to read the statements and see that they are free from obvious material errors and are presented in appropriate form. The CPA has the responsibility to request additional information from the client if the information received, on its face, appears incorrect or incomplete. Furthermore, a CPA may not ignore information, whether obtained from current work and data or from previous work, experience or training, which indicates that the financial statements are in error.

No longer will a presentation of financial statements be considered as either audited or unaudited.

While the accountant is required to present the financial statements in appropriate form, the appearance of the statements may or may not be a proper reflection of the underlying financial data. The phrase in the compilation report, *in the form of financial statements,* is intended to alert the reader that, even though the financial information may appear reliable, few procedures were performed.

The next level of assurance is that expressed by a review report based upon a review service. A review service relies primarily on information from management which has been subject to inquiry and analytical procedures. These procedures are substantially less than those in an audit because independent verifications and confirmations are not made; and yet, they are more than those in a compilation service. As a result, the CPA's report expresses limited assurance on the financial statements.

Review and compilation services are similar in that the procedures required are not sufficient for the CPA to assure the reader that all necessary adjustments and disclosures have been made.

Review services are similar to audit services in that, if the CPA firm is not independent, no assurance may be given. Independence is lacking when the CPA has a direct or material indirect financial interest in the entity being reported on. Note, however, that a CPA who is not independent can issue a compilation report as no assurance is given.

The highest level of assurance is that provided by an auditors' opinion. An audit opinion results from a review of internal control, tests of the accounting records, and examination and confirmation of the information in the financial statements.

The level of assurance needed is not determined by the time period covered by or the contents of the financial statements. Therefore, both interim and annual statements may be either compiled or reviewed. For example, the owner of a small owner-operated business may want an income statement quarterly to assist in planning for and managing the business. Since the owner is the person responsible for gathering the information, as well as for the reliability of the information, no further assurances may be desired. As a result, a compilation service would be adequate. However, if the same owner is reporting to a lender, such as a bank, and the lender wanted a higher level of assurance than a compilation report provides, the income statement could be reviewed. Similarly, at year end many businesses may want reviewed or audited annual statements to increase the realiability of the information even though services leading to a lower level of assurance may be useful and adequate for interim statements.

The standards and procedures provided by SSARS No. 1 also apply to reports for not-for-profit organizations. The statement provides that compilation and review reports may be issued on financial statements prepared in accordance with another comprehensive basis of accounting, so long as that basis of accounting is disclosed.

The Time to Decide

The issuance of SSARS No. 1 provides an opportunity for the CPA and the client to discuss and reconsider the type of service really needed. One factor to consider would certainly be the amount of the accountant's fee. The fee for a review service will most likely be more than that for a compilation service because the required procedures will be more extensive.

To insure that the CPA and the client are in agreement as to the type of service, level of assurance desired, and the resulting fee, an engagement letter is recommended. The engagement letter may specify the type of service to be performed, the anticipated wording of the CPA's report, a description of any additional services which may be desired, a description of the limitations of the engagement, an explanation of the fee arrangements, and an identification of the financial statement(s) along with other supplementary information, if any, that is to be covered by the CPA's report.

There are other reasons why it is important to determine the statement(s) to be covered and the level of assurance to be given before the CPA's work is begun. Basically there are restrictions on the CPA's ability to change an engagement from an audit to a review or a compilation. Before agreeing to a change, the CPA must evaluate the reasons for the change from an audit, the amount of added effort which would be required to complete the audit and the estimated additional cost to complete the audit. In any case, information regarding noncompliance with generally accepted accounting principles which may have come to the CPA's attention cannot be ignored in issuing a report.

Red Tape?

Is this new professional standard a way of increasing red tape and, conse-

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quently, increasing accounting fees? NO. The standard was developed to more closely reflect the level of services being performed and, per se, no additional financial statements nor financial statement disclosures are required by SSARS No. 1.

Departures from the full set of financial information that is collectively called "financial statements" are still permitted *if* disclosed properly in the accountants' report. For instance, if a client desires only an income statement, this new standard does not also require the presentation of a balance sheet, or footnotes. In such a case, the first two paragraphs of the CPA's report would be unchanged and a third paragraph would be added:

> Management has elected to omit substantially all of the disclosures, the balance sheet and statement of changes in financial position required by generally accepted accounting principles. If the omitted disclosures were included in the financial information presented, they might influence the user's conclusion about the company's financial position, results of operations, and changes in financial position. Accordingly, the financial statement presented is not designed for those who are not informed about such matters.[2]

The above modification is only one of a variety of such modifications. Statement No. 1 contains other examples that are too numerous to mention here.

Conclusion

During this time of transition[3], SSARS No. 1 will generate much discussion among CPAs, their clients and other financial statement users. The change will also present a special opportunity for a review of existing agreements between clients and CPAs. After exploring the various alternatives and restrictions of the new standard, clients will be able to select the service that more closely matches their needs. The CPA will be able to express a level of assurance that more closely reflects the conclusions reached. While instant understanding is not likely to occur, the changes and clarifications provided by Statement No. 1 should enhance the users' ability to understand the CPA's association with unaudited financial statements and, thereby, the credibility of the CPA. □

FOOTNOTES

[1]A nonpublic entity is one which is not required to file financial statements with a regulatory agency in connection with the sale or trading of its securities in a public market.

[2]Paragraph 21, SSARS. No. 1.

[3]The effective date of SSARS No. 1 is for periods ending on or after July 1, 1979.

Compilation and Review

Definitive Services

By Carol B. Hardan

Unaudited financial statements comprise a significant segment of the services provided by certified public accountants. For the past half century, the accounting profession has grappled with reporting procedures for both audited and unaudited financial statements. However, because the pronouncements with respect to unaudited financial statements were quite limited, the services performed by the CPAs issuing reports on unaudited financial statements varied greatly.

After careful consideration and in order to establish uniform standards, the American Institute of Certified Public Accountants has now issued "Statement on Standards for Accounting and Review Services No. 1".[1] This Statement provides for two levels of reporting by CPAs on unaudited financial statements. These two levels, compilation and review, as differentiated from an audit, are summarized in this article as a reference for financial statement users so that they may more readily recognize the degree of responsibility the CPA has assumed.

Compilation of Financial Statements

The first level of responsibility relating to unaudited financial statements is a compilation.

A compilation consists of presenting, in the form of financial statements, information that is the representation of management. The accountant does not express any assurance on the statements presented.

In order to perform a compilation of financial statements, the accountant should:

- Possess a level of knowledge of the accounting principles and practices of the industry in which the entity operates.
- Possess a general understanding of the nature of the entity's business transactions, the form of its accounting records, the stated qualifications of its accounting personnel, the accounting basis on which the financial statements are to be presented and the form and content of the financial statements. This knowledge ordinarily is obtained through experience with the entity or through inquiry of entity's personnel.
- Read the compiled financial statements and consider whether they appear to be appropriate in form and free from obvious material errors.

The accountant is not required to make inquiries or perform other procedures to verify, corroborate, or review information provided by the entity. However, if the accountant becomes aware that the information supplied by management is incorrect, incomplete or otherwise unsatisfactory, he or she should obtain additional or revised information or withdraw from the compilation engagement entirely.

The requirements relating to financial presentation and footnote disclosures are the same whether for

[1]"Statement on Standards for Accounting and Review Services No. 1, *Compilation and Review of Financial Statements*", effective for financial statements for periods ending on or after July 1, 1979.

audited, reviewed or compiled financial statements.

The recommended standard accountants' report applicable to compiled financial statements is shown in Exhibit I.

To the Board of Directors
of the Company

The accompanying balance sheet of XYZ Company as of December 31, 19XX and the related statements of income, retained earnings, and changes in financial position for the year then ended *have been compiled by us.*

A compilation is limited to presenting in the form of financial statements information that is the representation of management. We have not audited or reviewed the accompanying financial statements and, accordingly, *do not express an opinion* or any other form of assurance on them.

(Signed)

Date

(Italics have been added for this presentation.)

(Departures from generally accepted accounting principles and the effect on the financial statements, if known, should be disclosed in a separate paragraph of the accountants' report.)

Exhibit I

Review of Financial Statements

The second level of responsibility relating to unaudited financial statements is a review.

A review consists of performing inquiry and analytical procedures to provide the accountant with a reasonable basis for expressing limited assurance that no material modifications should be made to the statements in order for them to be in conformity with generally accepted accounting principles.

The objective of the review differs significantly from that of a compilation, where no expression of assurance is contemplated, and from that of an audit, which results in the expression of an opinion on the financial statements taken as a whole.

In order to perform a review of financial statements, the accountant should:

- Possess a level of knowledge of the accounting principles and practices of the industry in which the entity operates.
- Possess a general understanding of the entity's business.

Possessing a general understanding of the entity's business contemplates knowledge of its organization and operating characteristics, including production, distribution, compensation methods, types of products and services, operating locations and material transactions with related parties. It also requires knowledge of the nature of the entity's assets, liabilities, revenues and expenses. This understanding is ordinarily obtained through experience with the entity or its industry and by inquiry of the entity's personnel.

The inquiry and analytical procedures should ordinarily include the following:

- Inquiry concerning the entity's accounting principles and practices and the methods followed in applying them.
- Inquiries concerning the entity's procedures for recording, classifying and summarizing transactions.
- Inquiries concerning actions taken at shareholders' and Board of Directors' meetings.
- Inquiries of persons having responsibility for financial and accounting matters.
- Comparison of the financial statements with those of a comparable prior period or periods.
- Comparison of the financial statements with anticipated results, if available.
- Study of the relationships of certain interrelated accounts.
- Reading the financial statements to consider whether they appear to conform with generally accepted accounting principles.

The inquiries and analytical procedures to be performed in a review of financial statements are a matter of the accountant's judgment. In reviewing the accounting records the accountant may consider the following:

- The nature and materiality of the items.
- The likelihood of misstatement.
- Knowledge obtained during current and previous engagements.
- The stated qualifications of the

entity's accounting personnel.

- The extent to which a particular item is affected by management's judgment.
- Inadequacies in the entity's underlying financial data.

A review does not contemplate a study and evaluation of internal accounting control, tests of the accounting records or obtaining corroborating evidential material through inspection, observation or confirmation, since such procedures normally apply only in audits. Therefore, a review does not provide assurance that the accountant will become aware of all significant matters that might be disclosed in an audit.

However, if the accountant becomes aware of information that is inaccurate, incomplete or otherwise unsatisfactory, he or she should perform additional procedures to achieve limited assurance that there are no material modifications that should be made to the financial statements or withdraw from the review engagement.

The recommended standard accountants' report applicable to reviewed financial statements is shown in Exhibit II.

To the Board of Directors
of the Company

We have reviewed the accompanying balance sheet of XYZ Company as of December 31, 19XX, and the related statements of income, retained earnings, and changes in financial position for the year then ended, in accordance with standards established by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management of XYZ Company.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an examination in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, *we do not express such an opinion.*

Based on our review, *we are not aware of any material modifications* that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

(Signed)

Date

(Italics have been added for this presentation.)

(Departures from generally accepted accounting principles and the effect on the financial statements, if known, should be disclosed in a separate paragraph of the accountants' report.)

Exhibit II

Audits of Financial Statements

The objective of an audit is to provide a reasonable basis for expressing an opinion on the financial statements taken as a whole.

An opinion may be expressed only when the independent auditor has performed an examination in accordance with generally accepted auditing standards.

The opinion may be unqualified:

- The statements present fairly the financial position, results of operations and changes in financial position of the entity, and conform with generally accepted accounting principles applied on a consistent basis.

The opinion may be qualified:

- An exception is taken to certain items and such exception is disclosed.

The opinion may be adverse:

- The statements do not present fairly the financial position of the entity.

In an audit, the examination must be performed by a person or persons having adequate technical training and proficiency as an auditor. The auditor must make a proper study and evaluation of internal control and obtain sufficient competent evidential material through inspection, observation, inquiry and confirmation. The auditor must maintain an independence in mental attitude and exercise due professional care in the performance of the examination and in the preparation of the report. All work is to be adequately planned and assistants properly supervised.

The reporting standards may be considered self-evident in the accountants' report.

The accountant's unqualified report with respect to audited financial statements is shown in Exhibit III.

To the Board of Directors
of the Company

We have examined the balance sheet of XYZ Company as of December 31, 19XX, and the related statements of income, retained earnings, and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of XYZ Company as of December 31, 19XX, and the results of its operations and the changes in its financial position for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

(Signed)

Date

(Italics have been added for this presentation.)

Exhibit III

Table No. 1 provides a quick reference to the levels of responsibility that financial statement users may expect relative to each of the three levels of service.

	Compilation	**Review**	**Audit**
No assurance	X		
Limited assurance		X	
Expression of opinion			X
Standard footnote disclosures	X	X	X
Accountant's independence required		X	X

Table No. 1

The American Institute of Certified Public Accountants is continuing to refine the state of the art in the unaudited area. The Institute's Accounting and Review Services Committee has established the following new task forces:

- Task Force on other Accounting Services
- Task Force on Communication With Users When the Accountant Is Not Independent
- Clarification of Independence-Interpretations Task Force
- Task Force on Subsequent Discovery of Facts Existing at the Date of Compilation or Review Report
- Special Reports Task Force

It is interesting to note that the exposure draft on compilation and review drew more comment from the profession than any other pronouncement. Both the profession and the public may be encouraged by the effort now being expended in this area. □

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Management Advisory Services—Need for Definition

Questions of Propriety and Auditor Independence

By M. Zafar Iqbal

Revenue derived from management advisory services (MAS) constitutes a significant part of the total income of many public accounting firms. Though some accountants still find management advisory services hard to justify, most view it as a logical extension of their work in the financial field. All of the big auditing firms have committed their resources to provide such services; some more eagerly and wholeheartedly than others. The surrounding controversy nonetheless remains! The questions revolving around propriety of this role assumed by the CPAs have never been resolved, and recently intense and vigorous criticism of MAS has resurfaced. This is typified by the comments made by Mr. Harold M. Williams, Chairman of the Securities and Exchange Commission (SEC), before the AICPA Fifth National Conference on Current SEC Developments held in January 1978.[1] The SEC Chairman singled out independence as one of the key issues facing the accounting profession. Williams noted that the problem of independence "is one of the professional attitude, which cannot be legislated, although legislation will undoubtedly be resorted to if self-discipline fails." He further indicated that the SEC is studying the effect that management advisory services may have on the auditor's independence.

Clearly there is a need to define the concept and scope of MAS.

Auditing and Consulting

Although the term "management advisory services" has been coined recently for usage, this type of service has been rendered by the accountants since the early days of the profession.[2] The push of the big auditing firms in this area has been accelerated since the postwar years, especially during the last two decades. Although MAS is most emphasized in larger firms, it is also predominant in smaller firms, often in a less formalized fashion. A survey performed by the Roper Organization, sampling practice units of the AICPA, concluded that over ninety percent of the respondents indicated that their practice includes advisory services to the clients.[3]

Most practitioners have come to recognize and identify MAS as an integral and significant part of their practices. Writers who consider surrounding issues to be still unresolved, generally concede to the fact that from a practical standpoint elimination of MAS is improbable because it has become an interwoven part of CPA's activities.[4] However cognizance of the reality has not diminished the surrounding controversy, since the questions raised relating to compatibility of such services with auditing have not subsided. Ethical consideration such as independence, competence and incompatible occupations factors are justifiably considered too important to be ignored solely due to wide-spread practice.

Independence

Rule 101 of the AICPA Code of Professional Ethics prohibits a CPA from expressing an opinion on the financial statements of a company unless he/she and his/her firm are independent with respect to the enterprise.[5] Some members of the profession claim that independence is not impaired if a CPA performs both auditing and MAS because *advisory services* are not the same as *management services*. This rationalization appears to be based mostly on matters of semantics. For example, if the CPA screens candidates and recommends one of them to fill an executive level opening in a client company, these services are of a managerial nature. The fact that the CPA did not make the final decision is not a relevant factor. It is so because at many levels of an organizational hierarchy the responsibility may be limited to exploring the available alternatives and recommending one of them to higher level executives. The final decision is then made at that level. A corporate personnel director may screen applicants for a vice-presidential position and recommend a well qualified candidate to the president for the final decision. This illustration points out that it really does not matter whether the service provided by the personnel director (on company payroll) is called a "management service" or a "management advisory service". Any attempt to draw a distinction between the two terms will be an exercise in futility.

Essentially the problem boils down to a role conflict. A role conflict takes place when two or more concepts of role overlap to cause a contradiction in the role behavior expected from an individual by various groups.[6] Even if the CPAs have a clear conception of the distinction between advice to management vs. making decisions for management, the distinction may not be so obvious to the client. Thus there is risk of misunderstanding resulting from different perception of the same situation. Mautz and Sharaf express it quite eloquently:

> *There tends to come a time in any arrangement for management services*

A logical solution to role conflict lies in discriminate limitation of MAS to those areas which fall within the expertise of the CPA.

when the mutuality of interest of the consultant and the client becomes so significant that the accountant ceases to be independent in the sense that we feel he should be for auditing purposes. Management requests advice because it expects to use it; the consultant gives it to be used; the consultant knows that as a consultant he will be judged by the ultimate usefulness of his advice in bringing success to management's efforts. He has had a hand in shaping managerial decisions and will be judged by management on the same basis that the management itself will be judged. How then can he claim to be completely independent.[7]

Independence is of paramount importance for certified public accountant's role as independent auditor:

The independent audit leads to the expression of a professional opinion as to whether financial information furnished to stockholders, prospective investors, bankers and other credit grantors, is fairly presented. Obviously the extent to which the opinion of a CPA on financial statements will add to their credibility in the eyes of investors or credit grantors will depend on their confidence in his independence of professional judgment, his technical competence and his assumption of an ethical responsibility to the public as well as to his client.[8]

Some might argue that independence is a frame of mind. This statement is correct but incomplete. Intellectual integrity deals with independence in fact; but the auditor also has to be independent in appearance. In summary, one could argue that to expect a CPA to first make recommendations and later audit the outcome of his/her own recommendations with complete independence is perhaps presumptuous.

Competency

Rule 201 of the AICPA Code of Professional Ethics forbids a member from accepting an engagement for which he/she or his/her firm neither have the competency nor expect to acquire it during the engagement.[9] Certified public accountants perform some services which have close relationship to their expertise, e.g., financial planning, computer control systems, and setting-up the accounting system for a client; often though their MAS activities are in areas which are tangential or apparently out of their professional realm. Most of the Big Eight CPA firms have extensive staff in their MAS divisions and are eager to provide their clients literally any management services they desire. This may entail assignments, for example, in labor negotiations, personnel selection, executive compensation, new-product planning, factory design and layout, job evaluation, marketing, pricing and promotion strategies, setting-up new pension plans, tax shelter, and helping a client company defend itself against a takeover. Needless to say, this is by no means an all-inclusive listing of the type of services offered.[10]

Many individuals question whether CPAs have the credentials to make critical appraisals in areas such as those mentioned above. They wonder whether the public accounting profession has circumvented Rule 201 in approving management advisory services by its members.

Incompatible Occupations

Another applicable rule is Rule 504 of the AICPA Code of Professional Ethics. The rule states that a public accountant is not allowed to concurrently engage in any business or occupation which impairs his/her objectivity in rendering professional services or serves as a feeder to his/her practice.[11] Regarding the second criterion i.e., relating to "feeder", it is difficult to envisage a public accounting firm obtaining consulting business from its clients in areas such as marketing analysis, organizational studies, job evaluation and manpower planning, executive search, executive compensation, and a host of other non-accounting activities without first having established the reputation as a CPA firm. Fortunately, it is not the type of situation where one continues moving in circles in an attempt to find the answer whether the chicken came first or the egg. In the case of public accounting firms, their expertise and reputation as public accountants decidedly influence their clients and result in obtaining consulting work. Thus one may draw the inference that accounting and auditing practice acted as the feeder to MAS work later obtained by the accountants.

Need for Definition

The concept of management advisory services and its scope have never been clearly defined and understood by members of the profession. Consensus does not exist on the reasons why the profession has moved into MAS area. The existing explanations are hypotheses at best, and suffer from absence of systematic analysis.[12] The Commission on Auditors' Responsibilities (Cohen Commission) recently recommended that professional standards should be expanded and the conditions that present the greatest danger to independence should be identified; auditors should decline any engagement that may bias the audit function.[13] The report further recommended that public accounting firms should not engage in employment recruiting or placement of individuals who would be directly involved in the decision to select or retain auditors.[14]

Position Taken by Public Accounting Profession

In 1970 the American Institute of Certified Public Accountants organized its management advisory service activities in a senior technical division. The dual objectives of the division are to assist CPAs in performing MAS services, and to develop guidelines and standards for this area of practice. In December 1973 a study was authorized by the AICPA Board of Directors. The aim of the comprehensive study was to define the MAS body of knowledge for CPA firms and their MAS practitioners. The study, known as the MAS Body of Knowledge and Examination (MASBOKE) Project, was completed by a group of researchers at the University of Texas at Austin in 1976. It identified the following breakdown under the knowledge of organization functions and related disciplines: executive planning; implementation and control; finance and accounting; electronic data processing; operations; human resources; marketing; management science.[15] Unfortunately, the scope of the study did not allow an analysis of the issues concerning propriety of advisory services by

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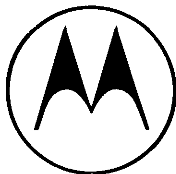

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public accountants. Perhaps it was considered unnecessary as the profession has assumed that MAS is here to stay. This hypothesis is substantiated by the fact that the Statements on Management Advisory Services were adopted by the Management Advisory Services Executive Committee in October 1974.

Conclusions

The public accounting profession has expanded its role in management advisory services. Quite often the activities in this segment of the practice appear to fall outside the boundaries of accounting and auditing. Many questions, especially those relating to independence, competence, and incompatible occupations, remain unanswered despite a long history of debate. Skeptics include even those who are well known as friends of the profession. For example, U.S. Senator Charles Percy recently noted:

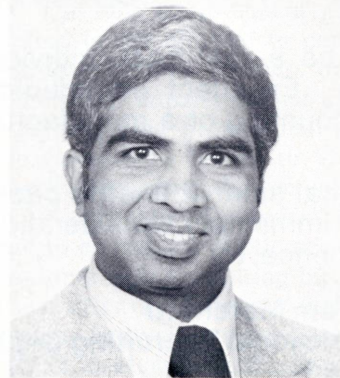
> *There may be conflict between some of these services and auditing. I think particularly in personnel placement there is conflict of interest. This is a big enough business, and an important enough profession, to this country that you don't have to go into a lot of unrelated activities.*[16]

The cynics might say that the profession tends to respond more quickly to critics rather than persuasion by friends like Senator Percy. Such an allegation could be rejected on the basis of good reasons. However for self-preservation and freedom from possible future governmental control it is critical that the profession make a concerted effort to define the concept and scope of management advisory services, once and for all, in the immediate future.

The above analysis indicates that it is necessary to remove any role conflict with the *raison d' etre* of the public accounting profession, i.e., auditing services. The most logical solution lies in discriminate limitation of MAS to those areas which fall within the expertise of the CPA, and can be identified as direct, natural extensions and adjuncts of auditing. Some of those activities include setting-up the accounting system, financial planning, computer control systems, internal controls in general, and tax planning. By focusing on planning and control aspects of sell-defined areas related to the financial field the CPA can continue to be of valuable service to the clients without violating, in appearance or in fact, the ethical rules relating to independence, competence and incompatible occupations. □

FOOTNOTES

[1]News Report, *The Journal of Accountancy,* February 1978, pp. 24-26.
[2]John P. Sullivan, "The Accountant as Consultant: A Historical Review," *The Journal of Accountancy,* November 1974, p. 92.
[3]Edward L. Summers and Kenneth E. Knight, "The AICPA Studies MAS in CPA Firms", *The Journal of Accountancy,* March 1975, p. 56.
[4]For example see William G. Shenkir and Robert H. Strawser, "Auditing and Management Advisory Services: A Conflict of Roles?", *Abacus,* June 1972, p. 19, and Benzion Barlev and Arieh Goldman, "Management Advisory Services and Accounting", *Abacus,* June 1974, p. 82.
[5]AICPA, *Code of Professional Ethics,* March 1975, p. 17.
[6]Billy J. Hodge and Herbert J. Johnson, *Management and Organizational Behavior: A Multidimensional Approach,* John Wiley & Sons, New York, 1970, p. 223.
[7]R.K. Mautz and Hussein A. Sharaf, *The Philosophy of Auditing,* American Accounting Association, 1961, p. 222.
[8]John L. Carey and William O. Doherty, *Ethical Standards of the Accounting Profession,* American Institute of Certified Public Accountants, 1966, p. 62.
[9]Code of Professional Ethics, op. cit., p. 18.
[10]For an extensive listing of Management Advisory Services See Pierre L. Titard, "Independence and MAS - Opinions of Financial Statement Users", *Journal of Accountancy,* July 1971, p. 50.
[11]Code of Professional Ethics, op. cit., p. 21.
[12]For a discussion of possible reasons see Barlev and Goldman, op, cit., pp. 74-82.
[13]Conclusions and Recommendations of the Commission on Auditors' Responsibilities, AICPA, New York, 1978, p. 100.
[14]Ibid., p. 101.
[15]"The MAS Body of Knowledge", *Journal of Accountancy,* April 1976, p. 81.
[16]"A Senator Speaks", *The Week in Review,* Haskins & Sells, Washington, D.C., March 10, 1978, p. 2.



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Audits of Federally Assisted Programs

Difficulties, Differences — and Opportunities

By Richard A. Scott and Rita K. Scott

There is a practice area of considerable size and importance that offers growing opportunities for Certified Public Accountants — audits of federally assisted programs. By the same token it can also be a quagmire that lies in wait to ensnare the unsuspecting who would enter without proper regard for its unique requirements and the risks[1] involved. This article is intended to point out some of the characteristic difficulties which attend these audits and to highlight certain basic differences from commercial engagements.

Identifying the Practice Area

The federal government distributes money and properties and provides technical and other assistance to a variety of units at the state and local level in the form of grants-in-aid, contracts, loans, loan guarantees, and insurance. Collectively they are referred to as "Federally assisted programs" and have been instituted by various pieces of legislation (Public Laws or "PLs"). More than one thousand programs are listed by the Office of Management and Budget (OMB) in the *Catalog of Federal Domestic Assistance.*[2] An estimated $72 billion will be provided this year to 50 states, 3,000 counties and nearly 90,000 cities and towns, as well as innumerable organizations closely associated with the federal government.[3]

Certainly the magnitude of these statistics is impressive. Perhaps even more impressive is the prospect for rendering professional service. By fiscal 1980 as many as 20,000 audits per year could result from the Comprehensive Employment and Training Act of 1973 (CETA) alone.[4] Many of the 39,000 General Revenue Sharing Trust Funds which participating governments have established to receive Federal monies will be audited by CPAs. Neither the federal, state, nor local governments are equipped to handle tasks of these proportions.[5] The opportunities for audit and MAS work are manifold.

The Federal Overseer

In 1973 President Nixon, by executive order, transferred administrative responsibility for Federal grants to the General Services Administration (GSA). In carrying out their responsibilities GSA issued a number of Federal Management Policy Circulars (FMCs) among which FMC 74-7 was particularly important; it contained standards for administering grants-in-aid. On December 31, 1975 the same administrative functions were transferred back to the office of OMB. They in turn revised FMC 74-7 and reissued it on August 24, 1977 as Circular No. A-102 (Revised).[6] A summary of significant changes contained in that document included a specification that grantee audits should be made in accordance with generally accepted auditing standards (GAAS) including the Government Accounting Office's (GAO's) *Standards for Audit of Governmental Organizations, Programs, Activities and Functions* (the "yellow Book"). The various Federal agencies charged with administering to the Government's assistance programs will apply these standards.

The Yellow Book Standards

How do audit standards contained in the Statements on Auditing Standards (SAS's) of the accounting profession differ from those of the yellow book? The GAO explicitly acknowledged the AICPA (American Institute of Certified Public Accountants) standards and subsumed them into their own. Insofar as standards for financial accounting and auditing are concerned there is substantial agreement between the two except where federal agency audit guides prescribe special principles at odds with those that are generally accepted. At one extreme a comprehensive basis of accounting other than GAAP may be encountered, in which case a special form of auditor's report is required.[7] In between that extreme and GAAP one may encounter departures from GAAP which call for an "except for" qualification of the standard auditor's report.

But there is a more important difference in audit standards; one that stems from the broad duties and responsibilities of GAO. Because GAO is a "watchdog" agency of the Congress it concerns itself with matters of legal compliance, optimal use of government resources, and the outcomes of legislative programs. These objectives are reflected in the yellow book's statement of audit scope. The scope of an audit includes three elements (hereafter referred to as a "comprehensive audit").

1. Financial examinations and evaluations of compliance.
2. Evaluation of economy and efficiency.
3. Evaluation of program results.

A financial examination is within the traditional realm of CPAs and was touched upon above. To date audits of federally assisted programs have been largely directed toward this facet.

Independent accounts will be impelled into a role that is less familiar than auditing in the traditional form.

However, government administrators and legislators are becoming increasingly concerned with management and program accountability. It seems reasonably safe to predict that the latter two elements which have heretofore been downplayed will grow in importance. Independent accountants will be impelled into a role that is less familiar than auditing in its traditional form.

Not all three elements are considered necessary in every instance, nor are they present in an unchanging degree of importance. It is critical at the outset, therefore, to clarify the audit scope with the contracting agency and to have it explicitly described in the engagement letter if it is not already specified in the audit guide.

Financial Examinations and Evaluation of Compliance

We mentioned earlier that CPAs are on familiar ground with respect to financial examinations. Fortunately, compliance reviews are also familiar to the independent accountant. The auditor is usually asked to ascertain whether a grantee has complied with laws, statutes and regulations which stipulate how funds are to be used. For example, procurement regulations requiring solicitation of bids and proper approval of contract change-orders are matters that are customarily reviewed in Environmental Protection Agency (EPA) construction grant audits.

The contracting agency has a responsibility to give the independent accountant sufficient guidance in these matters. Even so, it may come in a form that is difficult to work with or that is vaguely defined. The reader is urged to examine, as a case in point, the *Code of Federal Regulations*, Title 40, "Protection of Environment" which applies to EPA and the grants which it makes.[8] Or, an auditor may be asked to make a compliance review where the criteria are not defined in audit guides or other sources. Inadequate guidance with respect to the appropriate laws, rules, or regulations may compel the auditor to disclaim an opinion.[9]

Evaluation of Economy and Efficiency

The second element of a comprehensive audit involves determining whether government-furnished resources are being managed in an optimum manner. An independent auditor is not expected to render an opinion with respect to the economical and efficient use of resources entrusted to a grantee. Nor is a judgment expected concerning the performance of local management. The CPA is being asked to report upon specific procedures, methods, or activities that can be made more efficient or economical, and to make recommendations for bringing about changes. This entails issues such as the following:

1. Were expenditures really necessary?
2. Does duplication of efforts exist?
3. Are procurements made in economic order quantities, and are inventories at "lean" levels?
4. Is equipment operated at a high level of capacity?

Efficiency and economy should be viewed as relative terms, and thus their proximity to a maximum practicable level can be a subject of considerable disagreement. Clearly, the functions to be reviewed must be identified in the engagement letter and at no time should any assurances be given or implied concerning the overall operation of the entity.

Evaluation of Program Results

The federal legislation that gives birth to a program should set out the results and benefits that are anticipated. An appraisal of program results will evaluate the degree to which goals are reached, with proper regard given to the program costs involved. The strategies chosen, the directions taken, and how resources have been employed become important considerations. However, judgments concerning the wisdom of these actions will be extremely difficult to make. For them to be fairly made, criteria should be articulated by legislators or implementing agencies and promulgated to decision-makers. The criteria ought to be measurable, and a system of data gathering instituted to provide a basis for managing the program toward its intended goals, as well as for evaluating the extent to which goals are achieved. "Success measurements" should be audited, but as the reader probably suspects, the state of the art is as yet embryonic. To illustrate, consider a case in point.

A local government receiving an EPA grant for its air pollution control programs would be expected to enact ordinances to effect changes that will meet EPA's air quality specifications. It would also be expected to monitor and control air quality and to bring pollution levels within quality standards. There are several facets of this program that could be audited. Was appropriate monitoring equipment acquired, installed and put to work? Have policies been established for taking timely abatement action in the event that violations are observed? Are data gathering systems in effect for recording open burning permits, fuel conversions, and registration of major industrial and institutional sources of emissions? An inventory of emissions[10] taken periodically is an auditable set of measurements and is a significant determinant of program success, particularly when trends are considered. Another set of auditable measurements is the air quality monitoring data of pollutant concentrations such as sulfur oxides, carbon monoxide, and particulates in the atmosphere. National primary ambient air quality standards exist for defining unacceptable levels of these pollutants. Their monitoring entails taking readings of concentration levels at prescribe time intervals. The frequency and degree by which the standards are exceeded are objectively determinable facts that are subject to audit.[11] From this illustration the CPA's role emerges as potentially including activities such as:

1. Assisting in the design of control and information systems.
2. Assisting in the development of standards for measuring program results.
3. Audits of data on program activity which reflect the extent to which program goals are being attained.

GAO does not yet expect auditors to express an opinion on the success of programs, and CPAs should avoid giv-

ing wide-ranging assurances. At the same time it is well to remember that this is virgin territory and pioneering efforts could yield considerable rewards.

Other Considerations

The quality of accounting for federal funds is as varied as the governmental units themselves, and a correlation does not necessarily exist between unit size and excellence. On the whole, accounting information does not approach a quality level ordinarily found in business. Incomplete documentation and insufficient records often frustrate the auditor. A representative of one CPA firm arrived at a rural court house to find that all of the checks written during a period against a grant about to be audited had been inadvertently emptied into the incinerator by a porter. The entity employed a cash basis system to boot!

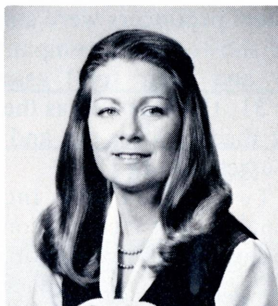
Audits may be conducted as much as several years after a grant is made, thereby making the situation more difficult to deal with. Compounding the problem, local personnel are often unfamiliar with the facts and circumstances surrounding the program because of high employee turnover. Furthermore, local personnel at times exhibit a lack of understanding of Federal grants and their compliance requirements. Record-keeping as a consequence often suffers. Auditors, too, can experience difficulties trying to cope with the myriad of audit requirements spelled out in dozens-upon-dozens of audit guides that have been issued by a plethora of federal agencies.[12]

In some cases independent auditors will be engaged by a local government unit, and in others by a federal agency. In the latter situation local government personnel tend to be guarded and mistrustful, and enlisting their assistance is difficult. The CPA is looked upon as an intruder sent there by Washington. On the other hand, auditors hired by local government authorities may be asked to make evaluations of economy and efficiency, and program results which could cast a critical light on the very persons engaging their services. Complicating matters even further, federal authorities expect CPAs to inform them of grantee deficiencies that are discovered, no matter who has engaged the auditors. It is like being caught between Scylla and Charybdis; whichever turn is taken can have troublesome consequences.

Conclusion

Federal assistance programs have created an excellent opportunity for practice development. Because the vast majority have June 30th year-ends, these programs can be serviced by the CPA during the traditionally slower months. Prospects for financial and compliance audits are very good, and the possibilities created by expansion of economy and efficiency audits and evaluations of program results make this practice area both attractive and interesting. Although the complications and pitfalls accompanying an engagement of this sort are very real and should be held in proper regard, they ought not to impede the accounting profession's response to a call for service. □

The quality of accounting for federal funds is as varied as the government units that use the funds.



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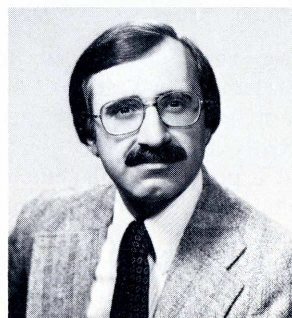

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FOOTNOTES

[1]For a discussion of some of these risks see: Robert H. Werner, "CPA Opportunities in Federally Assisted Programs," *The CPA Journal* (July, 1976), p. 12.

[2]A partial listing of the more significant programs may be found in: "Audits of Federal Government Programs: Annual Roundups," *Journal of Accountancy* (May, 1974), pp. 34, 36, 38.

[3]Elmer B. Staats, "Shortcomings With Grant Auditing and Suggestions on What Needs to be Done," Remarks made before the AICPA National Conference on Federally Assisted Programs, Washington, D.C., Nopember 8, 1977.

[4]*Ibid.*

[5]See for example: "Case Study — Illinois' Use of Public Accountants for Auditing State Activities," GAO Audit Standards Supplement No. 3. The appendix contains useful illustrations of written proposals, audit scope instructions, audit report content and form, and descriptions of auditor qualifications.

[6]"Uniform Administrative Requirements for Grants-in-Aid to State and Local Governments," *Federal Register*, vol. 42, no. 176, September 12, 1977.

[7]"Special Reports," *Statement on Auditing Standards No. 14* (AICPA, December, 1976), par. 4-6.

[8]See particularly: "Subchapter B — Grants and Other Federal Assistance."

[9]"Reports on Internal Control Based on Criteria Established by Governmental Agencies," *Statement on Auditing Standards No. 1*, (AICPA, November, 1972), Sec. 641.

[10]Emissions are registered as tons of pollutants entering into the atmosphere for a time period for a geographic area.

[11]For further detail see: "Illustrative Report, Air Pollution Control Program, Sassafras County, Maryland," GAO Audit Standards Supplement No. 6.

[12]See: Thomas R. Hanley, "Expanding Practice to Include Federally Assisted Programs Requires an Added Library Shelf," *Journal of Accountancy* (July, 1975), pp. 37-41.

Big Steel's Imbroglio

Illusory Profits and Real Taxes

By Sue Siferd and John Talbott

Financial publications would certainly lead one to place little credence in the contention that there is currently an erosion of business capital in this country, caused by confiscatory taxes, which is precluding industrial growth.

"These Republic Steel fourth quarter 1978 earnings were 60 cents above my estimate" confessed one analyst at a major brokerage concern.[1]

"Our most likely earnings estimates for 1979 assume 20 percent earnings gains for most of the major steel companies while our high end 1980 forecast shows earnings rising by another 50 percent," noted another.[2]

Despite the euphoria associated with such comments, it may be argued that in periods of inflation our existing tax laws provide for confiscatory tax rates well above the statutory limit. These confiscatory taxes stem from businesses' unwillingness and/or inability to deal with the inflation effect on earnings. What legislator in his right mind, for example, is going to vote for significant tax relief for corporations who continue to report record annual earnings?

Such earnings reports, in fact, are the basis of "obscene profit" remarks which appear to have led to an anti-business environment in the country at large. By masking the erosion of capital with spurious profits, significant tax reform is stymied. In essence, the time has come to realize that corporate external reporting, based on historic costs, is a major contributor to the stagflation affecting our country. The purpose of this article is to examine that contention.

The Study:

To support the position, 1977 annual reports and 10-K's of 13 major iron and steel producers were studied. Table One shows the 13 companies in our study and their total assets at December 31, 1977, as well as their reported net income after tax and their return on assets for 1977.

Table Two shows net income, replacement cost net income, common stock dividends, and excess of common stock dividends over replacement cost net income. Admittedly, the replacement cost figures generated via Accounting Series Release 190 are no panacea. Realistically, replacements will take place over many years and the new plant will provide additional revenue generating services and operating efficiencies. As a result, the replacement cost net income may paint a more dire picture than reality would warrant.

Bearing this caveat in mind, however, Table Two results are indicative of the erosion of business capital. Only four of the companies generated a positive replacement cost net income. Moreover, the common stock dividends for twelve of the companies exceeded the replacement cost net income. In fact, Carpenter Technology was the only company in the study whose common stock dividends did not exceed replacement cost net income.

Table Three compares the additional replacement cost expense as a percentage of income before tax, income after tax, and common stock dividends. For the twelve companies reporting an after tax profit, the additional replacement cost expense was at least one hundred percent for seven of the companies. Perhaps more informative, however, the replacement cost expense was no less than sixty percent of reported after tax income for any of the companies studied.

The staggering implications of these figures may be more readily understood if we arbitrarily assume that the "true" costs are only one-half as great as the reported replacement costs would indicate. Even under these assumptions, a significant portion of net income is illusory in nature and is neither available for dividends nor for capital expansion projects but is being clandestinely employed to replace higher priced plant, equipment and inventories.

In Table Four we have listed the primary earnings per share, replacement cost earnings per share, and dividends per share. In light of the fact that all corporations with the exception of Carpenter Technology were engaging in liquidating dividends, investors should cast a wary eye at the early 1979 market recovery of a number of the steel stocks.

The Trigger

This recovery, in fact, stems primarily from the subsidization of the steel industry through the "trigger" price mechanism which sets an arbitrarily high price for foreign steel. The combination of the trigger with high demand has raised steel prices sharply in an era when the administration anathema is inflation, and will exacerbate pricing problems for other U.S. industries that must employ steel in their manufacturing processes. More specifically, these industries will now find themselves at a similar competitive disadvantage with their foreign counterparts, as steel did earlier. While the exact impact on the economy as a whole is debatable, it is safe to assume that aggregate results are far from salutary as a result of subsidizing a particular industry.

The trigger price fiasco also demonstrates once again that historical costs which provide for illusory profits and confiscatory taxes in periods of rampant inflation are a nemesis to the economy in general. This is due, of course, to the way that the tax system handles depreciation. If a company spends $1-million on labor, it deducts the dollars against sales revenue of approximately equal purchasing power.

TABLE ONE
(Figures in 1,000's of Dollars)

Name of Company	Total Assets At Dec. 31, 1977	Net Income for 1977	Return on Assets
Armco Steel Corporation	$ 2,882,754	$119,832	4.16%
Bethlehem Steel Corporation	4,898,900	(448,200)(1)	-9.15%
Carpenter Technology Corporation(2)	263,999	33,753	12.79%
The Cleveland-Cliffs Iron Company	354,615	26,111	7.36%
Copperweld Corporation	268,083	16,307	6.08%
Cyclops Corporation	333,332	8,992	2.70%
Inland Steel Company	2,302,352	87,801	3.81%
Kaiser Steel Corporation	961,440	4,544	0.47%
Lukens Steel Company	188,241	12,070	6.41%
National Steel Corporation	2,827,646	60,125	2.13%
Republic Steel Corporation	2,406,330	41,031	1.71%
United States Steel Corporation	9,914,400	137,900	1.39%
Wheeling-Pittsburgh Steel Corporation	765,691	(25,630)	-3.35%
Totals	$28,367,783	$125,896	0.44%

(1) Bethlehem reported a loss of $120-million before taxes (a credit) and nonrecurring items; the nonrecurring item included a $750-million estimated cost of closedown of facilities.
(2) Fiscal Year ended June 30, 1978.
Source: 10-K's and Annual Reports, 1977.

TABLE TWO
(All figures in 1,000's of dollars)

	Net Income for 1977	Replacement Cost Net Income(1)	Common Stock Dividends	Excess of Common Stock Dividends over Replacement Cost Net Income
Armco	$119,832	($25,168)	$53,310(2)	$ 78,478
Bethlehem	(448,200)	(836,200)	65,500	901,700
Carpenter	33,753	12,353	10,216	(2,137)(4)
Cleveland-Cliffs	26,111	10,467	12,250	1,783
Copperweld	16,307	3,693	6,732	3,039
Cyclops	8,992	(31,977)	2,774(2)	35,781
Inland	87,801	(199)	52,654(2)	51,314
Kaiser	4,544	(76,009)	10,449(2)	86,499
Lukens	12,070	1,633	4,128	2,495
National	60,125	(42,875)	48,232	91,107
Republic	41,031	(137,492)	25,892	163,384
U.S. Steel	137,900	(362,100)	182,400	544,500
Wheeling-Pittsburgh	(25,630)	(75,204)	0(2) (3)	75,204

(1) Replacement Cost Net Income = Net Income minus Additional Replacement Cost Expense. Additional Replacement Cost Expense is determined from the 10-K reports and is the sum of the excess of Replacement Cost of Goods Sold and Replacement Cost Depreciation Expense, over Historical Cost of Goods Sold and Depreciation Expense. The tax effect of the Additional Replacement Cost Expense is not reported since such costs are not a deduction under present income tax laws. Appendix A reports this information.
(2) Also paid a preferred stock dividend.
(3) Paid one-half preferred dividend.
(4) Carpenter Technology Corporation is the only company in our study whose Common Stock Dividends did not exceed Replacement Cost Net Income.
Source: 1977 Annual Reports, 10-K's and our computations.
(5) The tax effect of additional Replacement Cost has not been considered in these computations because present Federal Income Tax Laws do not allow this expense as a deduction for tax purposes. See Appendix A for the hypothetical tax effect.

Corporate external reporting based on historic costs is a major contributor to stagflation in the economy.

If the company spends the same $1-million on a building, however, it will soon be matching the depreciation charge against inflated sales dollars of reduced purchasing power. The resultant products, of course, are spurious profits and excessive tax bills. While this process hurts all business, it is particularly detrimental to industries such as steel with lengthy capital turnover.

In an interview, *Forbes* magazine asked U.S. Steel's vice president-controller, Bracy Smith, whether the steel industry has been hurt by the fact that its profits were overstated. "I suspect that it has," Smith said, "because people say, 'Hell, you're making this much money; why do you need more?' "[3]

Politicians, of course, are extremely susceptible to this type of logic and their historical attitude toward steel over the past twenty-five years is ample indication of the ominous implications of fictitious figures.

In 1952, for example, Truman seized the steel industries to prevent what he deemed to be inordinate profits and a wage-price spiral. In 1962, Kennedy castigated U.S. Steel publicly over a proposed price increase of less than four percent and in 1972 Nixon heaped a great deal of "jawboning" on the industry. Of more recent interest was the initial Carter posture of disparaging steel over a proposed price increase which belatedly gave way to the trigger mechanism as layoffs in the industry increased and political pressure mounted.

Whenever demand for American steel placed the steel industry in a position to get higher prices and profits, the government forced it to settle for less.[4] Those decisions initially took their toll in such events as Bethlehem Steel's multi-million dollar write-off of its outdated Lackawanna, New York plant and will soon be causing economic dislocations as a result of market interference associated with the "trigger" prices.

Both types of events could possibly have been avoided with more liberalized depreciation rules or other tax policies which would have benefited the economy in general. The need for such policies is evident if one examines the replacement cost figures generated via ASR 190.

In essence, the dissemination of such figures via financial publications as opposed to their obfuscating position within 10-K's might have proved an impetus for tax reform which would have provided for a healthy domestic steel industry and obviated the need for the trigger mechanism which now threatens widespread economic dislocations.

Why Not Management:

Intuitively, one would expect management to adopt those accounting techniques which would reflect economic reality and strengthen the corporate position vis-a-vis ubiquitous governmental taxing units. On closer inspection, however, it appears that management often favors high fictitious earnings as opposed to lower real earnings and attempts to employ those apocryphal figures to cement its position within the company and to increase personal remuneration.

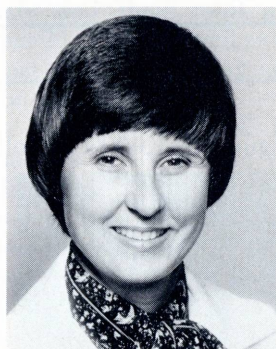
There have been several studies which corroborate these contentions. Duvall and Austin, for example, found that managers of firms with depressed earnings and stock prices are more likely to find themselves thrown out of office by dissident stockholders.[5]

Lee Seidler, of New York University, expressed it succinctly: "I would suppose the fact that management holds stock options and things of that sort may sway their judgment."[6]

Conclusion:

Reporting of inflated profits by industries such as steel has resulted in real tax rates of an inordinate magnitude which have diminished steel's competitive position vis-a-vis countries such as Japan whose tax system imposes no special burden on capital intensive industries. Moreover, pressures on corporate management in the earnings per share arena appear to have perverted the very group who should have lobbied for more liberal tax rules to combat the competitive decline.

The scenario that has developed in steel is actually somewhat frightening. A decline in a basic industry results in political pressure to subsidize the industry. These subsidization efforts in turn lead to a decline in competitive position for steel processors who in turn demand political help which further fuels inflationary force. As tables two, three and four indicate, the steel industry does need help. The crux of the matter is that profit figures reported by management appear to be one of the prime reasons that the help is in the form of triggers and not taxes. The resultant product may well be economic stagnation through protectionism.



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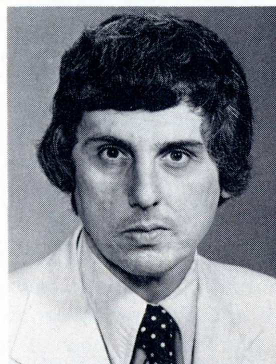

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NOTES

[1]"Heard on the Street," *The Wall Street Journal*, January 18, 1979, p. 37.

[2]*Ibid.*

[3]"Steel: Biting the Bullet," *Forbes*, December 1, 1977, p. 36.

[4]"Helping American Steel," *The Wall Street Journal*, October 17, 1977, p. 26.

[5]R.M. Duvall and D.V. Austin, "Predicting the Results of Proxy Contests," *Journal of Finance*, September 1965, pp. 464-471.

[6]"Steel: Biting the Bullet," *op. cit.*, p. 35.

TABLE THREE

Name of Company	Additional Replacement Cost Expense as a Percentage of (a) Income Before Tax	(b) Income After Tax	(c) Common Stock Dividends
Armco	119.2%	121.0%	272.0%
Bethlehem	— (1)	— (2)	592.4%
Carpenter	32.2%	63.4%	209.5%
Cleveland-Cliffs	39.7%	59.9%	127.7%
Copperweld	54.6%	77.4%	187.4%
Cyclops	326.5%	455.6%	1476.9%
Inland	96.2%	100.2%	167.1%
Kaiser	— (1)	1772.7%	770.9%
Lukens	47.2%	86.5%	252.8%
National	151.0%	171.3%	213.6%
Republic	429.9%	435.1%	689.5%
U.S. Steel	490.7%	362.6%	274.1%
Wheeling-Pittsburgh	— (1)	— (2)	0 (3)

(1) Reported loss before tax
(2) Reported net loss
(3) No common stock dividends issued
Source: 1977 Annual Reports, 10-K's, and computations.

TABLE FOUR

Name of Company	Primary Earnings Per share	Replacement Cost Earnings Per Share(1)	Dividend per Share of Common Stock	Average Number of Shares of Common Stock Outstanding
Armco	$ 3.80	($1.088)	$1.80	29,700,000
Bethlehem	($10.27)	($19.15)	$1.50	43,665,000
Carpenter	$ 3.97	$1.452	$1.20	8,509,000
Cleveland-Cliffs	$ 4.26	$1.709	$2.00	6,124,728
Copperweld	$ 2.91	$0.658	$1.20	5,608,000
Cyclops	$ 3.69	($15.29)	$1.30	2,158,394
Inland	$ 4.23	($.1086)	$2.60	20,267,000
Kaiser	$ 0.51	($11.00)	$1.50	6,996,891
Lukens	$ 4.68	($0.633)	$1.60	2,579,000
National	$ 3.12	($2.225)	$2.50	19,273,000
Republic	$ 2.54	($8.496)	$1.60	16,183,000
U.S. Steel	$ 1.66	($4.362)	$2.20	83,011,299
Wheeling-Pittsburgh	($ 7.70)	($20.17)	0	3,728,575

(1) Replacement Cost EPS = (Replacement Cost Net Income — Preferred Stock Dividend) divided by weighted average number of shares of common stock.
Source: Annual Reports, 10-K's, and computations.

APPENDIX A

(All figures in 1000's of dollars)

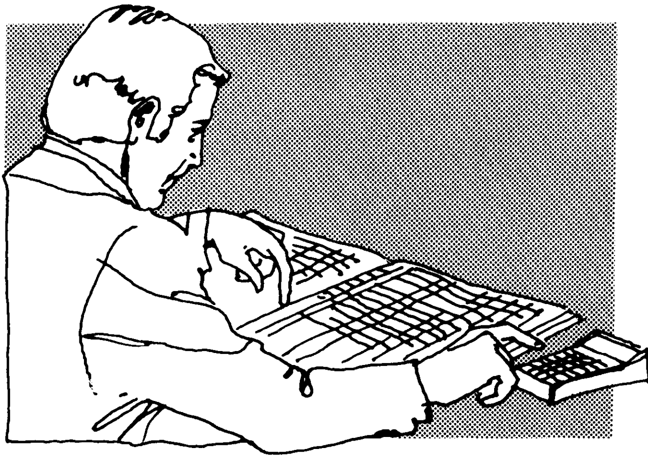
	Net Income for 1977	Replacement Cost Net Income net of Tax Effect [1]	Common Stock Dividends	Excess of Common Stock Dividends over Replacement Cost Net Income Net of Tax Effect [2]
Armco	$ 119,832	$ 44,432	$ 53,310	$ 8,878
Bethlehem	(448,200)	(649,960)	65,600	715,560
Carpenter	33,753	22,625	10,216	(12,409)
Cleveland-Cliffs	26,111	17,976	12,250	(5,726)
Copperweld	16,307	9,748	6,732	(3,016)
Cyclops	8,992	(12,312)	2,774	15,086
Inland	87,801	42,041	52,654	10,613
Kaiser	4,544	37,344	10,449	(26,895)
Lukens	12,070	6,643	4,128	(2,515)
National	60,125	6,565	48,232	41,667
Republic	41,031	(51,801)	25,892	77,693
U.S. Steel	137,900	(122,100)	182,400	304,500
Wheeling-Pittsburgh	(25,630)	(51,408)	0	51,408

(1) Statutory tax rate of 48% assumed.

(2) Replacement Cost Net Income net of tax effect exceeded Common Stock Dividends for Carpenter, Cleveland-Cliffs, Copperweld, Kaiser, and Lukens.

Appendix A has been prepared under the hypothetical assumption that all productive assets and inventories were replaced at their replacement cost. Under this assumption, additional Replacement Cost expense *would* be deductible for federal income tax purposes. Using the statutory tax rate of 48% for 1977, we have computed the Replacement Cost Net Income, net of taxes. As Appendix A illustrates, a comparison of common stock dividends with Replacement Cost Net Income net of tax effect shows eight of thirteen companies paying a common stock dividend in excess of Replacement Cost Net Income net of tax effect.

It should be further noted that because of Investment Tax credits, present and prior operating losses, losses due to discontinued operations, and other financial events, many of the steel companies did not pay taxes at the statutory federal income tax rate of 48% in 1977.



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Progress Toward International GAAP

The Barriers Are Formidable, But Are Yielding

By Carole Ann Elsea

The explosive growth of world-wide trade, the development of multinational firms, the establishment of international monetary bodies, and the global focus of investors have resulted in an increasing demand for an internationally uniform set of generally accepted accounting principles. Although progress had been made, the development and adoption of world-wide standards is a monumental task with a multiplicity of barriers.

Barriers

Barriers to international consistency in accounting encompass a wide range of factors:

- human nature
- cultural influences
- economic conditions
- legal requirements
- governmental rulings
- differences in national practices

Each will be discussed briefly, citing pertinent examples which contrast strongly with U.S. practices.[1]

Human nature is a strong barrier; individuals are intuitively inclined to resist change and its accompanying uncertainties; accountants are not exceptions to this general rule. Additionally, individuals exhibit even greater reluctance to accept changes which are perceived as "foreign" or "another country's way."

Cultural influences also inhibit conformity in accounting; widely diverse business practices and traditions have developed and are practiced throughout the globe. For example, in many Latin American countries cancelled checks are not documentary evidence of payment. Perhaps as a result of this tradition banks do not return cancelled checks to the issuer as a matter of course. Individuals and businesses must maintain official receipts of payment for taxes, governmental licenses, and other vital disbursements of cash.

Economic conditions present barriers to international GAAP as economic conditions have effected accounting principles and practices in some nations. Price-level adjustments are a specific case in point. Price-level adjustments to financial statements have been developed and are utilized in countries, such as Chile, Argentina, and Brazil, where inflation has soared to hundreds of percentage points within a few years. For over ten years Brazilian accountants have prepared balance sheet restatements of fixed asset costs by means of a government-calculated index. The net credit resulting from this reinstatement is recorded as a reserve in shareholders' equity.[2]

Other barriers to GAAP are legal systems and legal requirements. Some differences in business practices reflect nations' underpinning legal systems. Two major streams of legal thinking exist in Western nations: the Anglo-Saxon System of Case Law and the Napoleonic Code; far eastern and middle eastern countries, whose economic influence have grown dynamically in recent years, have yet other legal heritages which affect business and record-keeping.

Governmental rulings are a formidable barrier to international accounting principles. Governments may promulgate specific handling of business transactions which gives rise to one accounting treatment for taxes and alternate accounting treatments for financial reporting or securities disclosures. For instance, in stimulating capital investment some governments allow a very rapid write-off of new investments in plant and equipment. In Great Britain, for example, these new investments may be written off in the year in which they are made; this is a 100% immediate write-off.[3] The treatment of foreign exchange gains and losses is another area where some governments have mandated specific accounting methods in recent years.

Another barrier to the establishment of international standards is the development or lack of development of national standards.

Whether or not national standards are officially formulated, the historical, gradual development of accounting principles within individual countries has produced an incredible diversity in acceptable practices among nations.[4] Goodwill is a typical example of international inconsistency. In India the establishment of amortization of goodwill is not required; in Sweden and Peru goodwill which is capitalized need not be amortized until its value is obviously diminished.

Progress

In spite of these many barriers, encouraging progress has been made toward agreement and uniformity among the accounting practices of numerous countries. There is increasing comparison, discussion, and consensus among accountants for narrowing world differences.

Since 1926 there have been periodic meetings of the International Congress of Accountants which serves as an important forum for the discussion of international accounting issues. Delegates representing over fifty nations took a very positive step toward the unification of accounting by establishing the International Federation of Accountants (IFAC) at the eleventh congress in Munich, Germany, in October, 1977. (The next international congress will convene in Mexico City in 1982.) Although the Federation will not address the formulation of international principles, it will produce ethical, educational, and other non-technical international guidelines for the accounting profession. Early in 1979 it issued an exposure draft entitled *Ob-*

jective and Scope of the Audit of Financial Statements, which is to be the first of a proposed series of worldwide auditing guidelines.

Since World War II there have been regional meetings such as the Accountants International Study Group, (AISG) comprised of accountants representing Canada, the United Kingdom and the United States. The ASIG has served as a forum for discussion of accounting topics of concern to each and prepared ten comparative studies on broad subjects such as materiality and accounting for tax purposes. As a result of these studies, some degree of harmonization in accounting principles has been achieved in limited areas among the participating countries.

The International Accounting Association in North and South America, the Union of European Accountants, and the Conference of Asian and Pacific Accountants are other groups which have also played a role in bringing about the atmosphere of cooperation which exists today.

The most significant achievements toward the standardization of worldwide accounting principles have been those of the International Accounting Standards Committee (IASC) founded as a result of the Tenth International Congress of Accountants. The committee was formed in early 1973 by accountants from nine national accounting societies representing Australia, Canada, France, Germany, Japan, Mexico, the Netherlands, the United Kingdom and the United States. Today approximately forty countries ranging from Belgium and Fiji to Yugoslavia and Zambia are associate members of the group. All have pledged their "best efforts" in facilitating the adoption of IASC standards by the accounting bodies of their home countries.

To date the IASC has completed eleven standards with others in preparation. Those which have been issued concern these areas:

- disclosure of accounting policies
- consolidation of financial statements
- inventory valuation
- depreciation
- essential information for financial statements
- presentation of price changes and their impact
- statements of changes in financial position
- prior period items, and changes in accounting estimates and policies
- research and development
- contingencies, and events occurring after the balance sheet date
- construction contracts[5]

Some topics currently under study address research and development costs, and extraordinary items such as foreign currency translation.

Although these standards are not legal mandates they represent a significant advance toward the goal of internationally accepted accounting principles and they have had substantive impact. In Great Britain, for example, all listed companies on the London Stock Exchange are required to comply with IASC standards. The French Institute has officially adopted all IASC standards and enforces compliance with them by established disciplinary procedures. Another indication of IASC's influence is Japan's move in 1977 requiring companies to issue consolidated financial statements as suggested in the IASC standard for the consolidation of financial statements.

The growth of worldwide economic interdependency has prompted interest in international accounting standards by the United Nations. Specifically, the U.N.-sponsored study of "The Impact of Multinational Corporations on the Development Process and on International Relations" concluded that international accounting standards should be developed by accounting experts for multinational corporate financial reporting. The IASC has assumed this responsibility to date.

The Future

Although the barriers are formidable, accountants have made considerable progress toward the establishment of international GAPP. The International Accounting Standards Committee has issued eleven standards and the newly formed International Federation of Accountants will prepare guidelines on related areas of accounting such as ethics and education.

The authority of ISAC and IFAC pronouncements will be officially defined by more member nations. Some may accept international standards wholly; others, partially. In either case, the disclosure in financial statements of differences between national and ISAC recommended principles will likely be required.

Professional accounting organizations are serving as forums for their members' opinions, discussions, and recommendations and as sources of information for the latest international progress. These organizations and others throughout the world will also continue to provide representation for their members at the international meetings and in the organizations where international GAAP are being enforced. ☐

FOOTNOTES

[1]The following examples draw heavily upon Michael N. Chetkovich's address, "International Developments in Accounting and Auditing", presented November 29, 1977 before the Conference on Accounting for Multinational Entities at the University of Texas at Dallas.

[2]Lafferty, Michael, "International Moves in Inflation Accounting: A Convergence of Methods?," *The Accountant,* Vol. 176, No. 5324, (January 27, 1977), 106.

[3]"The Global Snares for Corporate Accountants". *Business Week,* (July 25, 1977), 162.

[4]Readers desiring further information are referred to the AICPA's 1975 guide to *Professional Accounting in 30 Countries* which contains descriptions of accounting principles used in each of the countries as well as sections concerning the country's forms of business organization, requirements for stock exchange listings, and other background information. Price Waterhouse & Company's *Guide for the Reader of Foreign Financial Statements* (George C. Watt, Editor, 2nd Edition January 1975) lists the primary differences in accounting principles between the United States and twenty-four countries in clear, concise form.

[5]Not all eleven are in effect as yet: IAS No. 9, *Accounting for Research and Development Activities, IAS* No. 10, *Contingencies and Events Occurring After The Balance Sheet Data,* and IAS No. 11, *Accounting for Construction Contracts,* become effective for financial statements covering periods beginning on or after January 1, 1980.

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Education

Faculty Evaluations

Value and Validity

Editor:
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For many years it has been the task of college teachers to evaluate students and to assign them a grade of A, B, C, D or F according to their performance. In more recent times, particularly since the student unrest of the midsixties, the students have in turn evaluated the teachers at many institutions, frequently also on a five-point scale and have assigned them grades of five to one. This evaluation by students is usually done on a standardized form. Some methods use class time toward the end of the semester, some require that the forms be mailed in toward the end of the semester or after the semester is over, and some require the evaluation be done in the early days of the following semester.

Typical of the items on which students rank their instructors are: "The instructor's objectives for the course have been made clear," "The instructor used class time well," "The instructor was readily available for consultation with students," "Lectures were too repetitive of what was in the textbook," "The instructor was enthusiastic when presenting course material," "The text was clear in presentation of concepts."

Some schools have designed their own forms and some have elected to use a standardized form and rating scale such as the Educational Testing Service form based on the Michigan State University scale, the form from the Berkeley Center for Research and Development on Higher Education, the Purdue Rating Scale for Instruction, or the Illinois Course Evaluation Questionnaire. The standardized forms have the advantage of being more thoroughly researched and of allowing comparability with other institutions. The self-developed forms are more adaptable to a particular situation and may be less expensive because they need not be purchased from an outside source.

Purposes of Faculty Evaluations

Basically there are three purposes of faculty evaluations: 1) to help faculty members improve their instruction techniques, 2) to guide students in their selection of courses and/or teachers, and 3) to assist administrators in their evaluation of the teaching abilities of individual instructors. To these purposes may be added a somewhat auxiliary purpose: 4) to conduct research on faculty performance.

The first purpose, that of assisting instructors in self-improvement, is certainly a worthwhile goal and was probably the first motivation toward faculty evaluations. Long before the days of standardized and compulsive evaluations, some teachers were designing and administering their own questionnaire in an honest attempt at improvement. Provided these faculty members were not so blind to their shortcomings that they failed to ask the right questions, they received meaningful information that assisted them in bettering their instruction techniques. However, the teachers that needed the most improvement were usually those that failed to ask for or ignored any kind of feedback from their students. Consequently, faculty evaluations were only made of some conscientious teachers who were motivated to improve, and they were probably good teachers anyway. In order to get the message across to the poorer teachers it was necessary to make the evaulations compulsory and to provide some sort of standardized form for general use. On the whole, the poorer teachers ignored the results from these evaluations as they ignored less formal forms of feedback.

The second purpose of faculty evaluations is to guide students in course and/or faculty selection. Using a faculty evaluation for this purpose formalizes a process in which students have always engaged and provides an information supply with equal access for all students. While formerly students had to rely on word-of-mouth or the informal files of a sorority or fraternity, they could now consult a handbook or their college library to obtain this information. This assumes, of course, that the results of evaluations were made available to students, which is not the case at all institutions.

The major objection to using faculty evaluations to guide students in their course and faculty selection relates to the confidentiality of the information. Some faculty members are sensitive about having their ratings generally known. Those who object to publishing faculty ratings point out that the confidentiality of student grades is protected by the Buckley Amendment and should not instructors have the same rights to privacy?

The third purpose of faculty evaluations is to assist administrators in their evaluation of teaching ability. This is probably the most controversial use of faculty evaluations. One has to sympathize with an administrator who must make decisions concerning promotion, tenure, and salaries given the

information at his/her disposal. Teaching, which is *the* major or at least *a* major activity of faculty, is not easily assessed. Self-evaluations by instructors have obvious difficulties. Classroom visits tend to provide very poor samples of performance besides being grossly unpopular. Achievement tests tend to apply only in courses stressing rote learning. Peer ratings sound good, but as far as classroom performance is concerned they can only be based on hearsay — which is what the administrator would probably base his/her evaulation on anyway. Given the alternatives, student evaluations of faculty seem the ideal answer.

Why then the strenuous objections by some faculty members to this method? Most of the objections center around validity. One proponent of teacher evaluations by students quotes from Aristotle's *Politics* which declares that we receive a better notion of the dinner from the guests than from the cook, likening the students to the guests and the teacher to the cook.[1] This may be true. However, the guests are far more likely to give an opinion based on flavor than on nutrition; and, in the long run, it is nutrition that counts. Opponents to this use of faculty evaluations say that students tend to give an opinion of a course or an instructor based on how much they enjoyed it rather than on what they learned from it. The charge is that faculty evaluations measure popularity rather than teaching ability.

The fourth purpose of faculty evaluations is to conduct research on factors related to faculty performance. This was listed above as an auxiliary purpose because most of the research done with faculty evaluations is to prove or disprove the validity of the instrument rather than assess performance. In other words, the research has been the result rather than the cause.

Validity of Faculty Evaluations

The most serious charge against faculty evaluation instruments is that they lack validity. That is, that they do not measure what they purport to measure — teaching effectiveness.

There are many factors that influence the rankings given by students in faculty evaluations. Where these variations are known and allowed for in the interpretation of the results, the rankings are still usable. Some of these factors relate to the questionnaire itself and the way it is administered. Students may react negatively to an overly long questionnaire. They are most likely to complete a questionnaire with clear instructions and easy to check answers.[2] Students may also react to teaching conditions over which the teacher has little control. In general, research has shown that lower-level courses, moderate-sized classes, and required courses tend to receive less favorable ratings.[3] Classes held during the middle of the day receive higher rankings than those held in the early morning.[4]

Dr. Fox and Other Interesting People

There are other factors that influence rankings that are more subtle and harder to allow for in the interpretation of rankings. Consequently, these defects are of a more serious nature. One assertion is that faculty evaluation results are unduly influenced by the "popularity" of the instructor. There are several studies that appear to confirm this.

Williams and Ware conducted a study in which they hired a Hollywood actor to deliver six types of lectures. The content density was high, medium or low. The manner of delivery was high expressive or low expressive. In the high-expressive lectures the actor used devices such as humor, enthusiasm, and voice modulation while not using them in the low-expressive lectures. Afterwards students were administered an achievement test and asked to rank the lecturer. As might be expected, high scores on the achievement test were associated with high content. High rankings of the lecturer were associated with high expressiveness. In Williams and Ware's early study in 1975, it appeared that high expressiveness also aided achievement, but this was not born out in a later study. The correspondence between high expression and high rankings of the instructor without regard for content is what the authors termed a "Dr. Fox effect."[5]

Keaveny and McGann (1978) did a study relating student ratings to certain behavioral clusters. Two clusters related to competence and organization which the authors labeled "Taut Ship" for high levels and "Loose Ship" for low levels. Another two clusters related to concern and consideration which the authors labeled "Nice Guy" for high levels and "Bad Guy" for low levels. As might be expected, "Nice Guy-Taut Ship" received the highest overall ratings and "Bad Guy-Loose Ship" received the lowest overall ratings. However, "Nice Guy-Loose Ship" had a better chance of a good overall rating than did "Bad Guy-Taut Ship", indicating that students appear to be more influenced by the consideration variables than the competence variables.[6]

Since certain variables appear to affect the outcome of faculty evaluations, one author has suggested that an instructor might use these effect to "cheat" on the evaluation. In a rather tongue-in-cheek article Michael Faia suggests:

> *As in the case of student cheating, the more interesting techniques are the more subtle ones. To begin with, we must make use of the findings of social psychology. For instance, research shows that course evaluations are influenced by a host of factors that have nothing to do with the "objective" aspect of teaching, such as whether or not professors are married, how they dress, whether they act "seductively" (as in the famous "Professor Fox" experiments), whether or not professors share the values of their students, whether or not students receive the grades they expect, whether or not instructors show "hostility."*[7]

Grade-Rankings Correlation

Besides the assertion that rankings are influenced by a group of behavioral variables that may loosely be characterized as "popularity", there is also the assertion that rankings are unduly influenced by the grade that a student receives or expects to receive in a course. This claim crops up over and over with good reason. A correlation between rankings and grades has occurred in many major studies.

Table 1 presents the findings from twenty-nine large grade-rating studies published between 1934 and 1974. Twenty-eight of the studies show positive correlations between grades given students and rankings given instructors. In total the studies represent more than 80,000 student ratings in thirty-five or more colleges and universities. The only study of this group which shows a negative correlation is the Heilman and Armentrout study which was done in 1935, and it is open to serious question from a control standpoint because the teachers apparently administered and handed in their own rankings.[8]

Table 1 does not present an exhaustive list of all the studies that have

TABLE 1
PUBLISHED DATA FROM 29 LARGE GRADE-RATINGS STUDIES
1934 — 1974

Author and Date of Publication	Maximum Grade-Rating Correlation Found
1. Anikeef (1953)	+ coefficient of .73 in freshman-sophomore classes
2. Bassin (1974)	+ coefficient of .10 affecting rankings to 32 percentiles
3. Bausell & Magoon (1972)	+ coefficient of .6
4. Centra & Linn (1973)	+ correlation; unstated "moderate" amount
5. Cornwell (1974)	+ correlation accounting for 11% of variance
6. Echandia (1964)	+ correlation at .01 level of significance; no coefficient given
7. Elliott (1950)	+ correlation on all 10 items on Purdue rating scale; no coefficient given
8. Granzin & Painter (1973)	+ coefficients of .14 to .21
9. Heilman & Armentrout (1936)	—coefficient of .04
10. Hildebrand, et al. (1971)	+ coefficient; unstated amount
11. Holmes (1971)	+ correlations: 5 to 11% of variance
12. Hudelson (1951)	+ coefficient of .19
13. Kennedy (1972)	+ correlation significant at .01 level; no coefficient given
14. Kooker (1968)	+ correlation at .001 level; no coefficient given
15. Mirus (1973)	+ coefficient of .85
16. Nichols & Soper (1972)	+ coefficient of .53
17. Overturf & Price (1966)	+ coefficient of .17; questionable statistical method used
18. Perry & Baumann (1973)	+ correlation of .78
19. Rayder (1968)	+ coefficient of .18
20. Rosenshine, et al. (1973)	+ correlations of .09 to .27
21. Rubenstein & Mitchell (1970)	+ correlations of .09 to .44
22. Spencer & Dick (1965)	+ coefficient of .85 to .91 in one study; + correlation of unstated amount in second study
23. Starrack (1934)	+ coefficient of .15
24. Stewart & Malpass (1966)	+ correlation significant at .001 level; no coefficient given
25. Voeks & French (1960)	+ coefficients up to .60 in one study; + correlations in 9 of 10 departments in second study; indeterminant results in third study because of faulty design
26. Walker (1969)	+ coefficient of .48 by rank order
27. Weaver (1960)	+ correlation significant at .001 level; no coefficient given
28. Powell (1974)	+ coefficient of .73
29. Powell (1975)	+ coefficient of .79

Source: Robert Powell, *College English,* January 1978, pp. 628-629.

been done in the area of faculty evaluations, and there are studies that demonstrate negative or no correlation between rankings and grades. However, some of these studies were done by evaluation consultation services which have a vested interest in proving the validity of their tests. Some other studies involve situations in which the teacher did not control the students' grades. Some negative correlation studies or no correlation studies were very small involving as few as one teacher. (This can also be said of some studies which found positive correlation although all those that appear in Table 1 involve at least five teachers.)[9]

Attempts to Establish Validity

The claim of lack of validity is indeed a serious claim and this claim has not been adequately refuted by the proponents of teacher evaluations. Attempts to deal with the problem have taken several forms. Consider, for example, the statement from a book published by one firm specializing in

evaluation programs, which presents three methods for testing validity:

> *The validity of an instrument, or whether it measures what it purports to measure, has been studied extensively for some instruments. Other institutions pilot test their own instruments, and may test the validity by requesting the same information in a variety of ways on different items, and then seeing if the answers are statistically consistent ... Validity is often measured by comparing a test intrument with one that has already established its validity. Many committees decide that face validity is acceptable; that is, the instrument logically appears to be valid.*[10]

The first method of testing for validity, that of asking for the same information in a variety of ways, is certainly a useful way to establish validity although its use with a single instrument is limited due to considerations of length. However, as regards the second method, testing an intrument with another valid instrument is not possible until it is established that there is a valid standard for teacher evaluations. Accepting a questionnaire on the basis of face validity, the third method, is like an auditor giving a clean opinion of a balance sheet because the figures add up. Equally unimpressive are items on the survey form such as "I have given thoughtful consideration to the questions on this form,"[11] which only prove the student read the item.

Conclusions

Teacher evaluations have been used for four purposes — for teacher self-improvement, for student guidance in selecting teachers and/or courses, for assessment of teachers' performance by administrators, and for research purposes. It appears that teacher evaluations do have some use for teacher self-evaluation particularly in regard to single items asked on the forms. For example, if a teacher consistently gets low rankings on an item such as "Spoke with expressiveness," he or she can strive for improvement in that area. Interpretations of overall rankings should be tempered by the knowledge that variables other than teaching effectiveness do affect these rankings.

Use of faculty evaluations by students to select courses is a valid use although permission of the instructor should be obtained in order to respect the confidental nature of the rankings. For the typical student seeking a professor and/or course the rankings are probably fairly accurate, assuming his or her goals and reactions will be similar to those of previous students. For the student with atypical goals and reactions, the rankings will be less useful.

Use of faculty evaluations by administrators is probably unwise in view of the lack of established validity. It is particularly hazardous to compare one faculty member's rankings with those of another faculty member. If it is desired to assess teaching effectiveness, then achievement tests administered to students appear to be more to the point, although achievement tests have problems also. Perhaps the only feasible alternative at present is to continue to rely largely on more objective measures of performance such as publications, offices held, committees chaired, etc. If and when more valid teacher evaluation instruments are developed, then they can be utilized. Re-testing the present survey forms appears to be of limited value because most have been tested extensively, and their validity is still in question. More research needs to be done to develop better measures of teaching effectiveness, perhaps utilizing achievement tests or some combination of achievement tests and student rankings. □

NOTES

[1]Richard I. Miller, *Developing Programs for Faculty Evaluation.* San Francisco: Josey-Bass Publishers, 1974, p. 30.

[2]William J. Genova et al., *Mutual Benefit Evaluation of Faculty and Administrators in Higher Education.* Cambridge, Mass.: Ballinger Publishing Co., 1976, p. 29.

[3]Ibid.

[4]Miller, p. 66.

[5]Reed G. Williams and John E. Ware, Jr., "Validity of Student Ratings of Instruction Under Different Incentive Conditions: A Further Study of the Dr. Fox Effect, "*Journal of Educational Psychology,* Vol. 68, No. 1, pp. 48-56.

[6]Timothy J. Keaveny and Anthony F. McGann, "Behavioral Dimensions Associated with Students' Global Ratings of College Professors," *Research in Higher Education,* December 1978, Vol. 9, pp. 333-345.

[7]Michael A. Faia, "How — and Why — to Cheat on Student Course Evaluations," *Liberal Education,* March 1976, Vol. LXII, No. 1, p. 118.

[8]Robert Powell, "Faculty Rating Scale Validity: The Selling of the Myth," *College English,* January 1978, Vol. 39, No. 5, pp. 616-619.

[9]Kenneth Elbe and Robert Powell, "Comment and Response," *College English,* January 1979, Vol. 40, No. 5, p. 564.

[10]Genova, p. 29.

[11]Student Reaction to Instruction and Courses (IDEA), Center for Faculty Evaluation and Development in Higher Education, Manhattan, Kansas, 1975.

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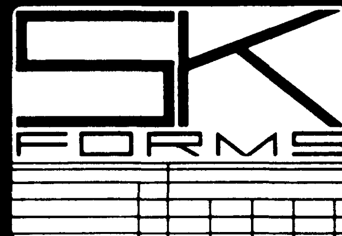

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FASB Statement of Financial Accounting Concepts No. 1

Objectives of Financial Reporting by Business Enterprises

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For many years the accounting profession has been derided for operating without a conceptual framework, or a constitution as it were. Although *APB Statement No. 4* was an attempt to grapple with the problem, the main thesis of Statement No. 4 was to describe the *status quo* rather than to prescribe how things should be.

In 1973 the Trueblood Committee authored a document entitled *Objectives of Financial Statements.* This document listed twelve objectives which provided the frame of reference for the FASB's *Statement of Financial Accounting Concepts No. 1, (SFAC No. 1)* issued in November 1978. The purpose of this article is to discuss *SFAC No. 1.*

Background

SFAC No. 1 is the first definitive statement of a series designed to provide the framework for the issuance of financial accounting and reporting standards. *SFAC No. 1* emphasizes profit-oriented enterprises; other types of entities are being considered in another phase of the conceptual framework project.[1] *SFAC No. 1* does not include any conclusions related to the measurement process, the form of statements, or the relative merits of various accounting models, e.g., historical cost vis-a-vis replacement cost. Rather, the Statement provides the concepts from whence future accounting standards will be drawn.

According to *SFAC No. 1,* financial reporting is not only affected by the environment within which it operates, but also by the characteristics and limitations of the information that financial reporting can provide. This results in approximate rather than exact measures, which is in contrast to the aura of precision that appears to surround financial statements. Moreover, financial statements are based on historic events although management may communicate soft information regarding the future, e.g., forecasts. Financial reporting does not pertain solely to financial statements; it also includes other means of communication that may be a product, directly or indirectly, of the accounting system. Admittedly, financial statements are the principal means of communicating accounting information. In certain cases more useful information can be provided by financial statements, whereas in other situations, the user is better served by means of financial reporting other than financial statements. Since information is used and provided at a cost, the benefits expected should usually equal or exceed the cost incurred.

The potential users of financial information include owners, lenders, suppliers, potential investors and creditors, employees, management, directors, customers, financial analysts and advisors, brokers, underwriters, stock exchanges, lawyers, economists, taxing authorities, regulatory authorities, legislators, the financial press and reporting agencies, labor unions, trade associations, business researchers, teachers and students and the public. The potential users are commonly dichotomized into two groups, external users and internal users. Since internal information can usually be tailored to the needs of management, reporting to internal users is considered beyond the scope of *SFAC No. 1.* Thus, the objectives of the Statement are designed to meet the needs of external users who lack the authority to require the financial information needed from an enterprise.

Although the focus of the Statement is largely on investors and creditors, recognized is the fact that other users can also benefit from information provided to these two particular groups.

Objectives of Financial Reporting.

SFAC No. 1 emphasizes that the goal of financial reporting is to provide information for investors, creditors and others who use the information for decision making. While the information should be a useful tool in reaching decisions, the role of financial reporting is only that of providing evenhanded, neutral and unbiased information to readers.

"Investors and creditors" is a broad term and encompasses not only those who deal directly with an enterprise and those who work through intermediaries, but also those who deal directly with other investors and creditors. "Investors" can be either equity securityholders or debt security holders. "Creditors" includes suppliers of goods and services as well as contractual lenders. Security analysts, lawyers, regulatory agencies and others who advise or represent the interests of investors and creditors are examples of intermediaries.

Financial information is a tool and can be either used or abused. What is more, understanding by investors, creditors, or other potential users may vary greatly. Nevertheless, proper use of this tool can be learned. The Statement concludes that financial report-

ing (a) is for the nonprofessional as well as for the professional; (b) should be able to be understood by the user who has a reasonable knowledge of business and who is willing to study the information provided, and (c) must be used properly.

More specifically, the information provided in financial reporting should aid present and prospective investors, creditors and other users in evaluating the amounts, timing and risk attached to prospective cash flows whether from dividends, interest or the proceeds from sale, redemption, or maturity of securities. In the final analysis, the test of the success of an investment depends on whether the investor receives more or less than the cash outlay. In a successful venture the investor receives not only the return *of* the investment, but also a return *on* the investment. An investment decision is really a choice between the receipt of cash today and the receipt of cash at a later point in time. Thus, rational investors, creditors and others need information to enable them to form decisions on expectations regarding risk and return. This same information is useful within the enterprise itself as it makes its own investment decisions.

Furthermore, financial reporting should provide information about resources, obligations and owners' equity; however, financial accounting is not designed to establish directly the value of a business.

Financial reporting should convey information about an enterprise during a particular period of time with primary focus upon earnings and its components. Investors, creditors and others try to derive expectations about the future partially by making extrapolations based on the past. Since investors, creditors and others rely on earnings information to predict the future, a cash basis approach cannot be considered an adequate basis for determining the past success or lack of success of an enterprise. Instead, accrual accounting is a better system for making predictions about future cash flows. Over the long run (the life of the enterprise) total net cash receipts equal total earnings. But in the short run, the essential difference between accrual and cash accounting is the timing of recognition of those items that comprise earnings.

The reported earnings and other information is used in various ways. For example, earnings information may be used in evaluating management, predicting earnings and evaluating risk. It is not the purpose of financial reporting to make the evaluations, but merely to provide basic information for such analyses.

Financial reporting should provide information relating to liquidity and solvency. In that respect, information about economic resources, obligations and owners' equity may be useful.

In evaluating management's stewardship and performance, earnings information is usually used for assessment purposes. However, earnings for a single period may not be sufficient for evaluating management's performance. In other words, enterprise success or lack of success is composed of many factors, external and internal. To say that current management is wholly responsible for earnings may not be correct, for the actions of past management may, in fact, have had an effect on the current year's performance. To break the whole into parts in order to evaluate the performance of management is difficult, since performance is an interaction of numerous factors. Management, however, can aid the communication process by providing explanations whenever necessary to make the results more meaningful.

Conclusion

SFAC No. 1 is a basis, inasmuch as the accounting profession is provided with a foundation upon which standards will be developed. This Statement provides the objectives of financial reporting with emphasis on economic resources of an enterprise, the claims to those resources and events that may trigger changes. Left unanswered are questions related to the measurement process, the form financial statements may take, and the trade-off of reliability and objectivity vis-a-vis relevance. However, these issues will be the subject of future phases of the conceptual framework project.

[1]The FASB issued a *Discussion Memorandum*, "Objectives of Financial Reporting by Nonbusiness Organizations," in June 1978. Public hearings were held in October and November 1978.

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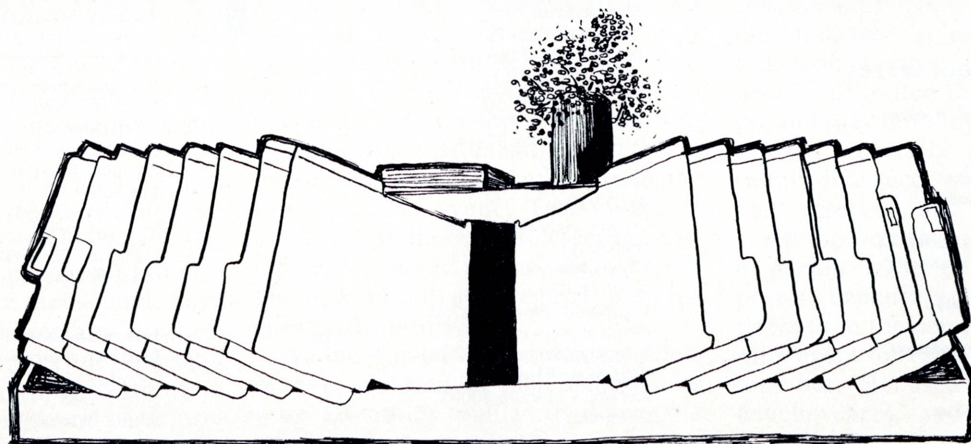

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Editor: Imogene A. Posey, CPA, CMA
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The Managerial Woman, Margaret Henning and Anne Jardim, Doubleday, Garden City, New York, 1977 $7.95.

It is reassuring to learn that the patterns of social conditioning for males and females are not necessarily fixed. However, the impact of different socialization is real and explains why many women experience "culture shock" when they enter the unfamiliar environment of the business world.

Henning and Jardim trace the patterns of difference and their implications directly to the job. They present the typical female/male attitudes toward responsibilities, pressures, opportunities for advancement, and the ability to identify a career future within a business organization. They correlate these attitudes to childhood and adolescence social experiences.

The most valuable activity in preparing one for successful adult life in the business world is team sports. Parents have long realized this valuable heritage and steered their sons into aggressive physical activity and the acquisition of outdoor skills. In team sports boys learn many psychological skills and strategies that will be used later in the business world: (1) what competition is, (2) what it feels like to win — to lose, (3) that you win as a team, not as a lone individual, (4) that there are risks, lots of risks, (5) how to handle pressure and stress when the game is close, (6) how to take criticism — from coach, peers, the crowd, (7) team work — working with people one wouldn't choose as friends outside the team, (8) hard work — preparation and practice brings the desired results, (9) a sense of belonging, of being part of something bigger than oneself — group identity, (10) if knocked down, the player has to get up again, (11) teams need a leader because motivation or lack of it depends on the coach, (12) all games have rules and once learned the rules you can be bent by influencing the referee, the coach, (13) all plays involve alternative plans and strategies.

Men, upon entering the business world, immediately perceive the similarities between team sports and the business environment and fall into line. Women, on the other hand, have not learned the necessary business skills from jumping rope, playing jacks, and cuddling dolls. Nothing in their cultural background has prepared them for what they face. Their reactions and responses to the business environment are those of a person in "culture shock."

Another barrier, according to the authors, that prevents women from climbing the corporate ladder is the lack of a role model. Men have done the job for hundreds of years, thus there is no doubt in the minds of the men who manage corporations that men are capable. Men's ambitions are supported since they brought legitimacy with them. Even the less bright have to prove by their performance that they do not belong. In effect, they have to prove failure.

Women, on the other hand, are illegitimate as they have never been part of the power structure. They have to prove over and over by their performance that they do belong. In effect, they have to prove success. Without a role model, even women sometimes find it difficult to believe in themselves and often state, "I can't do this because women before me have never done it."

The Henning and Jardim book is not an emotional recollection of their own lives, but rather it is the outcome of joint research on the personal and professional lives of twenty-five women who made it to the top of corporations — as vice-presidents and presidents in major industries. The authors trace the lives of the twenty-five subjects through childhood, adolescence, college, early career, and career maturity. Definite strong and regular patterns emerge from this study.

All the women were either the eldest or only children or their experiences were essentially similar to those of a first-born child. Their fathers were the dominant figure in their lives, they had extremely close relationships with their fathers, and they were involved in a wide range of activities traditionally considered masculine. The fathers did not reject their daughter's femininity, but rather, placed the highest emphasis on their developing the traditional sex role or behavioral style. Their parents were friends rather than superiors or autocrats. The openness of their relationships with their parents encouraged them at a very early age to deal with adults on a person-to-person basis, thus they developed confidence very early in dealing with authority figures. Their self concept as a free and autonomous persons was developed through the support and confirmation of the family. Although the assumption of feminine inferiority existed, it did not apply to them as individuals.

When these women entered the business world, similar work and relationship patterns appeared. Their pursuit of careers dominated most of their time even at the expense of personal relationships. None of them married until they were at least thirty five years old. Communication with their male peers was limited to the only common ground they felt they shared, work and the job. Generally, men perceived the twenty-five successful women as being cold, reserved, and aloof.

All the women had male mentors — a person who became father, supporter, encourager, teacher, and her strength in the company. He "acted as sales agent for the woman wherever he sent her. He used his reputation to develop hers, and his respect from

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others to gain acceptance for her. In times of direct confrontation with any group or individual, he would act as a buffer and place himself between the woman and her opponent."

This book is especially essential for men who manage corporations, not only to understand the problems of women at work, but also, to understand the ego and psychological problems facing men whose masculine identity is being threatened by having to share their power with women. "Masculinity is itself rooted in the acquisition of competence and achievement." Henning and Jardim present the idea that men's reaction to women's invasion of the business world is more typical of any threatened person rather than male chauvinism.

Additionally, the authors discuss how men join together in order to preserve their concept of masculinity. They "join together to sabotage women who have tried to succeed at the management level. If threatened by law that either they welcome the outsiders (women) into their midst or be punished for failure to do so, the insiders (men) can make their system work so as to avoid either outcome entirely."

Women & Power, Jane Trahey, Avon, New York, 1977. Paperback, 1978, $2.25.

"Women miss out on the moves upward for two major reasons: (1) men don't want them to move upward; (2) they are not as aware as they should be about how to play the power game. For the most part they don't even know there is a game. How can they possibly know the rules?" Women have never had any power, thus they do not understand what it is or how it functions.

Every page of Trahey's book vibrates with a blazingly energetic presentation of the tart details of the real world of business. As the reader follows the common problems and dilemmas of working women seeking careers at the top, it becomes clear why Trahey's book was selected by four major book clubs.

Trahey shares with us portions of her personal experiences which leave the reader with an indelible impression of a spunky, brave, and resourceful woman. In addition to her own experiences, her statements and conclu-

sions are based on the interviews with nine "queens" in the business world — women who chucked the corporation and struck out on their own.

We read of common themes in the lives of women who finally obtained that invisible force which gives one the freedom to take on the world — power! All the women grew up in an environment where females were strong and brave. Their mothers, all working women, were the dominant figures in their lives. All the women worked long hard hours; their lives revolved around their careers. The social engineering of Trahey's group of successful business women is directly opposite of the women interviewed in the *MANAGERIAL WOMAN.* The latter women had successfully climbed the corporate ladder, and each had a close relationship with her father. They received the social engineering that is usually accorded a son in the American culture.

All the women had male mentors — a person who believed in them, pushed them along, spoke up for them, and often arranged important contacts for them. Their male mentors provided the required open approval through their expressions of support.

The book ends with its author recommending the entrepreneurial path as the surest way for women to obtain power. You "no longer have to fight politics." Trahey's dream for women is positive but it underscores a cruel reality: most men groom other men to fill their positions.

Jewell Lewis Shane, CPA
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Replacement Cost Disclosures: A Study of Compliance with the SEC Requirement, Melvin C. O'Conner and Gyan Chandra; National Association of Accountants, New York, N.Y., 1978, 310 pp.

In an effort to provide information about compliance with and reaction to ASR 190, the National Association of Accountants initiated a series of replacement costing research projects in 1976. The results of the first two research projects were reported in *Effects of SEC Accounting Series Release No. 190 on Companies and Investors* (June 1976) *and Replacement Costing: Complying with Disclosure Requirements* (February 1977). This third, and concluding, study in the series consists of four sub-projects.

First, a detailed case study of nine firms, varying in size, structure, and diversity of operations, provides specific information on the various procedures employed in estimating current replacement costs for inventories, productive capacity, accumulated depreciation and depreciation expense, and cost of sales. For seven of the firms, a comparison is made between current procedures (as of May 1977) and planned compliance (as stated by the firms in a September-October 1976 interview). In addition to the expressed general doubt by the firms about the usefulness of replacement cost data, either internally or externally, the study reports that firms estimated the cost of compliance at approximately $100,000 (estimates ranged from $15,000 to $360,000).

The second sub-project reported in the study consisted of the examination of the 10-K forms and/or annual reports of 474 companies (covering 47 industries), for the purpose of "identifying experiences and problems individual corporations have encountered that are worth sharing with others." The study presents the results of the examination in both graphical and tabular form on an industry basis and for all firms in the survey. Of particular interest in this section of the study is the inclusion of 27 excerpts from annual or 10-K reports, vividly demonstrating the diversity of disclosure that firms have used. An alphabetical list of the companies surveyed, with the industry classification the authors employed, is provided. The authors also furnish references to similar studies which readers could use to supplement this study.

A third sub-project involved a questionnaire survey of 1,059 firms, from which the authors received 591 usable responses. The questionnaire (which is reproduced in the study) consisted of 28 questions designed to determine, for example, the firm's understanding of ASR 190, the manner in which implemented, level of management involved, opinion regarding usefulness, and comprehension of "current value." The reader will find the raw percentages of responses to each question and summary statements of questionnaire findings particularly informative. For example, 58% did not consider replacement cost data useful to management, 65% thought such data to be too subjective, and 50% saw no uses for the data. Further, the divergent views concerning the meaning of "current value" led the authors to include 451 verbatim responses to the question.

The final sub-project included in this study involved a questionnaire survey of 342 Chartered Financial Analysts (CPA's), with 80 usable responses. The questionnaire (reproduced in the study) consisted of 22 questions designed to determine the value of replacement cost disclosures to financial statement users. In a manner similiar to that employed in presenting the company responses, the authors provide a question-by-question analysis as well as a series of summary statements regarding questionnaire findings. To cite an example, 34% of the respondents viewed replacement cost disclosure as having no effect on investors, while an equal percentage felt that investors will be more cautious as a result of the disclosure. The authors note that the CFA's understanding of the meaning of "current value" are "so widely divergent that they defy generalization." Consequently, the study includes 32 verbatim responses to the question.

This study is strictly descriptive, leaving any conclusions to the reader. The authors have carefully avoided the inclusion of subjective evaluation or statistical analysis (except for raw percentage summaries). The research report is well-organized and unusually readable. To those responsible for compliance with ASF 190, the study should provide exceptionally valuable information concerning what others are doing to comply, how they are doing it, and their expectations about the future of replacement cost requirements in financial statements.

Clarence E. Fries
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