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Editorial

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Editor

EDITORIAL

Misuse of Accountants' Reports

There has been much comment because prospectuses and other literature issued prior to the flotation of securities have so frequently failed to indicate whether or not the affairs of the companies concerned have been subjected to independent investigation. In other cases when audits have been made there have been only incomplete and often misleading summaries of the accountants' figures and findings.

In the interest of all concerned it should be a fixed rule that securities in which the public is asked to invest should be supported by statements showing the results of impartial examination conducted by reputable practitioners.

The ideal condition would be the publication of the accountant's complete certificate, but in no case should there be any condensation which eliminates essential facts.

Often in these days one reads that John Doe, president of the company, supplies the following information. Of course, presumably, John Doe is an honest and honorable man, but as an interested party he cannot be completely impartial. The element of self-interest therefore will incline him to magnify the merits of the proposition and to deal gently with its demerits.

Frankly, we imagine that many investors must hesitate a long while when they find that an offering is compelled to rely upon the ex parte assertions of company officers. In particular an industrial concern which does not present an impartial reflection of its financial condition should never receive the encouragement of public subscription to securities.

The Journal of Accountancy

Stock exchanges could do much, if they would, to bring about a needed reform following the lines of the English companies' act or similar legislation in force in Canada and other British possessions.

It is not sufficient, however, that there be an independent audit, unless the public is sure that the accountant's findings are truthfully conveyed to possible investors. It is really worse than no report at all if vital figures are omitted or qualifications in the certificate are suppressed.

Incidentally a duty rests upon accountants to require clients and their bankers to make a fair use of their reports or certificates. Unless they do this they are morally responsible to the public for any misrepresentation in regard to which they do not exhaust every corrective remedy.

As an illustration of the use of an accountant's name in a way that might mislead the public, it is instructive to consider a recent prospectus, one paragraph of which reads somewhat as follows:

"Our accountants are John Smith & Son of Boston, who have audited our books for the last two years. All statements given, except for the year 1919, of which an audit is about to be made, are supplied by public accountants of high standing employed by us prior to our association with John Smith & Son."

In other words, the company leads the public to believe that its affairs have been audited by John Smith & Son, and that a clean bill of health has been given. As a matter of fact, the paragraph quoted means absolutely nothing except that John Smith & Son have conducted an audit—and it is quite possible that the accounting firm found it necessary to damn the whole financial condition of the company. There is no copy of the certificate, and the figures which are given are apparently in no wise connected with the accountants' investigation.

An unthinking prospective investor glancing over the prospectus to which we refer might be forgiven if he came to the conclusion that the financial affairs of the company had been investigated and their soundness endorsed by the well-known and reputable firm of John Smith & Son.

This is a misuse of the accounting profession against which the entire membership should vehemently protest.

Federal Registration of Accountants

Three or four years ago Edward N. Hurley, then chairman of the federal trade commission, propounded a scheme for the registration of accountants throughout the country under a federal regulation.

The idea met with considerable favor, particularly among government departments, and some members of the accounting profession who gave the matter only a superficial consideration expressed the thought that the plan had merit.

The American Institute of Accountants, through its committee on federal legislation, made emphatic protest against anything in the nature of federal regulation and succeeded in convincing the sponsors of the movement that it would be entirely undesirable.

Quite lately, however, there has been a recrudescence of the registration idea. There have been so many so-called tax experts and violations of the canons of decency that we fear there may be honest souls who may be convinced that something in the nature of federal regulation is imperative. Consequently, it may not be out of place to point out some of the essential fallacies of the idea.

If there were federal registration or regulation in any other form it might not be undesirable, provided the selection of the men and women to be registered were entirely detached from politics. For example, if the selection of qualified practitioners were to rest with the American Institute of Accountants and C. P. A. boards of states in which C. P. A. legislation is properly administered, no great harm might accrue.

Can anyone acquainted with official Washington imagine a bureau entrusted with the registration of accountants becoming anything more than a meeting place for congressmen and other politicians whose constituents desired registration? Anyone familiar with the way in which postmasterships are handed out may form a slight but inadequate idea of the political pressure which would bear upon the registrar of accountants. Every congressman from the back woods and the plains would have a constantly increasing number of friends "back home" seeking the prestige of federal registration. Probably many men who had never even been bookkeepers would shortly be registered as federal accountants, and it might easily follow that states in which there

The Journal of Accountancy

was practically no accounting work to be done would boast a register of accountants coextensive with the census.

It is all very well to say that registration could be carried out without consideration of the requests of congressmen and others, but no one who is familiar with official facts would believe such a statement.

The accounting profession is quite capable of managing its own affairs free from the dictates of politicians. The American Institute of Accountants was formed chiefly because the issuance of certified public accountant certificates had come so largely under the control of political powers. Anything in the nature of federal regulation would be reverting not only to conditions which preceded the formation of the institute, but to something infinitely worse.

What seems to us a far more desirable plan would be federal registration of incompetent accountants. If the government would make note of slipshod, inefficient and fraudulent work done by persons posing as accountants or tax advisors and would take some means to protect the public against charlatans, it would be accomplishing something. Congressmen would not be so anxious to seek registration of their friends on such a list.