

ACCOUNTING RESEARCH

Panel Discussion

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The invitation to participate in this discussion today suggested that each speaker explain current and future research plans of his organization.¹ For my part it seems appropriate to discuss the Commission's interest in the research that is being done in accounting and the extent of our participation in it.

Webster defines research as "Studious inquiry or examination; specif. and usually, critical and exhaustive investigation or experimentation having for its aim the discovery of new facts and their correct interpretation, the revision of accepted conclusions, theories, or laws, in the light of newly discovered facts, or the practical applications of such new or revised conclusions, etc.; also, a particular investigation of such a character or a book, article, or the like, presenting the investigator's discoveries; as, to give one's full time to research; Pasteur's researches in disease prevention."

"What is Research?" is the title of the first chapter in a book devoted to "Research Methods in Public Administration."² The author distinguishes research from formalized study of textbooks. Further he notes: "A tendency is sometimes evidenced to regard basic and applied research as distinct and separate activities. Some would even go so far as to assume greater virtue for the former, an attitude which occasionally smacks of snobbish superiority and exclusiveness. The disciples of this cult evidently feel that an immediate utilitarian objective contaminates the research process. However, a realistic appraisal would seem to indicate that

¹ The Securities and Exchange Commission, as a matter of policy, disclaims responsibility for any private publication by any of its employees. The views expressed herein are those of the author and do not necessarily reflect the views of the Commission or of the author's colleagues on the staff of the Commission.

² John M. Pfiffner, The Ronald Press Company, New York, 1940.

basic and applied research are difficult to separate in fact. The recent history of science and industry offers many examples where the improvement of an industrial process has resulted in noteworthy discoveries bearing on basic scientific principles. . . .”

These quotations seem to offer an adequate basis for believing that much of the work of the Commission in review and criticism of financial statements may be deemed to be a form of research in accounting. The Commission’s interest in accounting principles and their application, auditing standards, and financial reporting needs no elaboration as effective administration of the Securities Acts demands attention to these subjects.

It is significant, I think, that Commissioners and staff members have cooperated with the American Accounting Association, as well as with the other organizations represented here today, since the earliest days of the Securities Acts. My office files reveal, for example, that Mr. Carman G. Blough, the first Chief Accountant, was a member of the advisory committee on the preparation of “A Tentative Statement of Accounting Principles” and made a number of comments on the draft after consulting with Commissioner Mathews, who was charged at the time with general supervision over accounting matters for the Commission.

Mr. Blough’s successors have participated in one way or another in the development of successive statements by the Association. In addition, Mr. Earle C. King, when Chief Accountant, was a member of the Study Group on Business Income which reported its findings under the title “Changing Concepts of Business Income.” More recently the Commission has indicated clearly that it has a vital interest in the work of the Accounting Principles Board of the American Institute of Certified Public Accountants and in the research work of the American Accounting Association.

This is an appropriate occasion to refer to the discussion of consistency in the application of accounting principles which took place at the Fiftieth Anniversary celebration of the American Institute where Mr. Blough responded to a question and said in part:

“As a matter of fact, I think I have emphasized at numerous times that the policy of the Securities and Exchange Commission was to encourage the accountants to develop uniformity of procedure themselves, in which case we would follow. We expected to be able to follow the better thought in the profession and only as a last resort would the Commission feel the necessity to step in.”³

These remarks were made a few months after the Commission “announced a program for the publication, from time to time, of opinions on accounting principles for the purpose of contributing to the development of uniform standards and practice in major accounting questions.”⁴ The fourth release in the Accounting Series, published in April 1938, stated the Commission’s administrative policy with respect to financial statements. This series of releases and the instructions as to financial statements found in the various forms reflect the result of much accounting research on the part of the staff and consideration of comments from persons interested in, and also those who are affected by, our work. The original instructions as to form and content of financial statements were prepared with the assistance of experts and in 1940 were reexamined in the same way and published as Regulation S-X, which in turn has been reviewed, amended in part, and extended as conditions required.

The last major revision of Regulation S-X was completed in 1950. Preliminary drafts of the revision circulated for comment included statements on accounting principles which had been expressed in Commission opinions and had been followed by the staff in preparing

³ The American Institute of Accountants, Fiftieth Anniversary Celebration, 1937, p. 190.

⁴ Accounting Series Release No. 1, April 1, 1937.

comments on their review of financial statements. These proposals were severely criticized by many individuals and officially by the American Accounting Association and the American Institute of Accountants. The latter organization sent a special committee to appear before the Commission to urge that our regulations be framed in such a manner as to not interfere with the continued development of accounting principles by the accounting profession and the business community. The Commission agreed, except on one point on which a compromise solution was reached.⁵ It was understood at that time that the Institute would accelerate its efforts to narrow areas of difference and inconsistency in accounting practices, and to further the development and recognition of generally accepted accounting principles. This objective of the Committee on Accounting Procedure of the Institute is stated in paragraph 5 of the introduction to the “Restatement and Revision of Accounting Research Bulletins.”

Some of our critics say that progress has been too slow, while others say that insistence upon certification in accordance with generally accepted accounting principles is a barrier to progress. At the last annual meeting of the Association many of us heard Mr. Louis H. Penney, the president of the Institute, answer the question “Why Research?” In his discussion he mentioned the growing pressures from various sources for greater uniformity in statement presentation and observed that it might be a calamity of the greatest magnitude to the accounting profession if some government agency dictated the form and arrangement of financial statements and the principles to be followed in their preparation.⁶

In our work at the Commission we encounter various degrees of competence in accounting as in other professional work. Registrants and professional experts look to our prescribed forms and regulations for guidance. Drafting and revision of these publications

⁵ Accounting Series Release No. 70, December 20, 1950.

⁶ The Accounting Review, January 1960, p. 3.

requires continued study and, if you please, research. Projects requiring attention now include a general revision of Regulation S-X. This, as I have mentioned, was last accomplished in 1950. Assembling suggestions for a preliminary draft and exposure of the result to expert criticism takes considerable time, so no immediate results may be observable here. These preliminary steps, however, have been taken for a revision of Article 7 applicable to insurance companies other than life and title, and for a new, much needed article for life insurance companies. Similar work is partially completed on financial statements for employee stock investment plans. All of this work progresses slowly while the staff is more than fully occupied with an unprecedented volume of business in all areas under the Commission's jurisdiction.

A general revision of Regulation S-X is an opportunity to consider deletion of material which may be obsolete, to clarify those instructions which experience shows may need it, and to consider the substitution of new terminology for old. It is a time when the prescribed form and content of the financial statements must be judged against persistent requests for acceptance of alternate solutions and concurrent demands for greater uniformity. Emphasis in some circles on cash flow reporting suggests that the time may be ripe for prescribing some form of statement of source and application of funds in addition to balance sheets, income and surplus statements.

The Commission's report form for brokers and dealers is in the form of a financial questionnaire and conforms to the requirements of the New York Stock Exchange. Except for a revision in the minimum audit requirements applicable to monthly investment plans, this form has not been changed since 1942. Any revision of this form requires collaboration with special committees of the American Institute of Certified Public Accountants and representatives of the New York Stock Exchange. First steps, however, have been taken.

I have avoided a listing and discussion of problems in the field of accounting principles which require attention, as I am sure these will be mentioned by others on the program. We do want to participate in efforts to solve them.

Commissioner Robert E. Healy addressed the annual meeting of the Association at Atlantic City in December 1937 on "The Next Step in Accounting."⁷ Some of the steps he mentioned have been taken. Even our severest critics should agree that much has been accomplished since then. Commissioner Healy's closing sentences are appropriate now: ". . . The Commission will continue to recognize the propriety of the profit motive in our present system, the necessity of industry to acquire capital through the issuance and sale of securities, the impropriety of acquiring that capital, that is, other people's money, by misrepresentation or by anything short of fair and frank disclosure of all the important facts. We shall continue to seek and, when it seems wise, to rely upon the cooperation and advice of accountants, lawyers and representatives of industry. We shall try to be honest enough and brave enough to turn back when we discover we are on the wrong track. We ask you to recognize, as we do, the difficulty of deciding many of our problems. We ask you to help us. We want you to write to us and to talk with us, to give us your advice and your ideas. * * * As teachers of accounting, as students, as scientists in this complex business world of ours, your contributions can be of especial value. The task is worthy of the best there is in us. If it fails to bring us much money, let us remember as Emerson told the students at Dartmouth many years ago: 'Truth also has its roof, and bed, and board.'"

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⁷ The Accounting Review, March 1938, p. 1.